Legislative Proposals and Explanatory Notes Relating to Income Tax

Published by
The Honourable Paul Martin, P.C., M.P.
Minister of Finance

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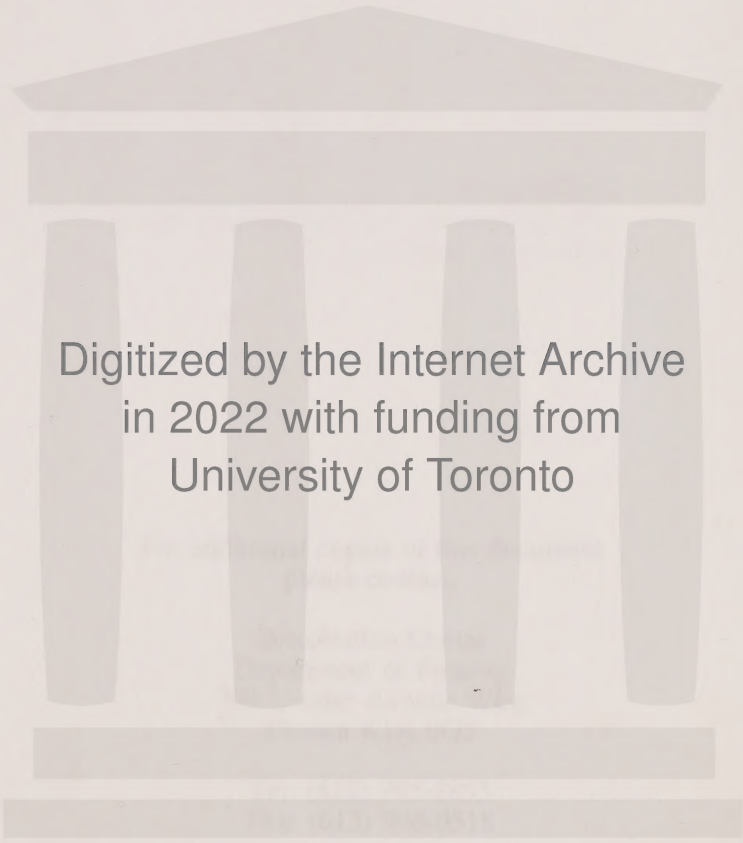

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SCHEDULE I

DRAFT LEGISLATION

PART I

1997 BUDGET AMENDMENTS

INCOME TAX ACT

1. (1) Paragraphs 12(1)(*z*.1) and (*z*.2) of the *Income Tax Act* are replaced by the following:

Qualifying environmental trusts

(*z*.1) the total of all amounts received by the taxpayer in the year as a beneficiary under a qualifying environmental trust, whether or not such amounts are included because of subsection 107.3(1) in computing the taxpayer's income for any taxation year;

Dispositions of interests in qualifying environmental trusts

(*z*.2) the total of all amounts each of which is the consideration received by the taxpayer in the year for the disposition to another person or partnership of all or part of the taxpayer's interest as a beneficiary under a qualifying environmental trust, other than consideration that is the assumption of a reclamation obligation in respect of the trust;

(2) Subsection (1) applies to taxation years that end after February 18, 1997.

2. (1) Subsection 18(11) of the Act is amended by striking out the word "or" at the end of paragraph (*f*), by adding the word "or" at the end of paragraph (*g*) and by adding the following after paragraph (*g*):

(*h*) making a contribution into a registered education savings plan,

(2) Subsection (1) applies to the 1998 and subsequent taxation years.

3. (1) Paragraphs 20(1)(*ss*) and (*tt*) of the Act are replaced by the following:

Qualifying environmental trusts

(*ss*) a contribution made in the year by the taxpayer to a qualifying environmental trust under which the taxpayer is a beneficiary;

Acquisition of interests in qualifying environmental trusts

(*tt*) the consideration paid by the taxpayer in the year for the acquisition from another person or partnership of all or part of the taxpayer's interest as a beneficiary under a qualifying environmental trust, other than consideration that is the assumption of a reclamation obligation in respect of the trust; and

(2) Subsection (1) applies to taxation years that end after February 18, 1997 and, for the purpose of paragraph 20(1)(*ss*) of the Act, as enacted by subsection (1), each contribution made after 1995 and before February 19, 1997 by a taxpayer to a trust (other than a mining reclamation trust as defined in subsection 248(1) of the Act) is deemed to have been made on February 19, 1997.

4. (1) Subsection 37(12) of the Act is replaced by the following:

Misclassified expenditures

(12) Where a taxpayer has not filed a prescribed form in respect of an expenditure in accordance with subsection (11), for the purposes of this Act, the expenditure is deemed not to be an expenditure on or in respect of scientific research and experimental development.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

5. (1) Paragraph 38(*a*) of the Act is replaced by the following:

(*a*) subject to paragraph (*a*.1), a taxpayer's taxable capital gain for a taxation year from the disposition of any property is 3/4 of the taxpayer's capital gain for the year from the disposition of the property;

(*a*.1) a taxpayer's taxable capital gain for a taxation year from the disposition after February 18, 1997 and before 2002 of any property

is 3/8 of the taxpayer's capital gain for the year from the disposition of the property where the disposition is the making of a gift to a qualified donee (as defined in subsection 149.1(1)), other than a private foundation, of a share, debt obligation or right listed on a prescribed stock exchange, a share of the capital stock of a mutual fund corporation, a unit of a mutual fund trust, an interest in a related segregated fund trust (within the meaning assigned by paragraph 138.1(1)(*a*)) or a prescribed debt obligation;

(2) Subsection (1) applies after February 18, 1997.

6. (1) Subparagraph 39(1)(*a*)(v) of the Act is replaced by the following:

(v) an interest of a beneficiary under a qualifying environmental trust;

(2) The portion of subsection 39(5) of the Act before paragraph (*a*) is replaced by the following:

Exception

(5) An election under subsection (4) does not apply to a disposition of a Canadian security by a taxpayer (other than a mutual fund corporation or a mutual fund trust) who at the time of the disposition is

(3) Subsection (1) applies to taxation years that end after February 18, 1997.

(4) Subsection (2) applies to the 1991 and subsequent taxation years.

(5) For the purpose of subsection 39(4) of the Act, where

(*a*) an election referred to in that subsection is made by a mutual fund corporation or mutual fund trust in prescribed form on or before its filing-due date for its taxation year that includes the day on which this Act is assented to, and

(*b*) the election is in respect of a particular taxation year that ends after 1990 and that is not after the corporation's or trust's taxation year that includes the day on which this Act is assented to,

the election is deemed to have been made in the corporation's or trust's return of income under Part I of the Act for the particular year.

7. (1) Section 40 of the Act is amended by adding the following after subsection (1):

Gift of non-qualifying security

(1.01) A taxpayer's gain for a particular taxation year from a disposition of a non-qualifying security of the taxpayer (as defined in subsection 118.1(13)) that is the making of a gift to a qualified donee (as defined in subsection 149.1(1)) is the amount, if any, by which

(*a*) where the disposition occurred in the particular year, the amount, if any, by which the taxpayer's proceeds of disposition exceed the total of the adjusted cost base to the taxpayer of the property immediately before the disposition and any outlays and expenses to the extent they were made or incurred by the taxpayer for the purpose of making the disposition, and

(*b*) where the disposition occurred before the particular year, the amount, if any, claimed under paragraph (*c*) in computing the taxpayer's gain for the preceding taxation year from the disposition of the security

exceeds

(*c*) such amount as the taxpayer claims in the taxpayer's return of income for the particular year, where

(i) the disposition occurred in the 60-month period that ends at the end of the particular year,

(ii) the taxpayer is not deemed by section 110.1 or 118.1 to have made a gift of property before the end of the particular year as a consequence of a disposition of the security by the donee, and

(iii) at the end of the particular year and throughout the following taxation year the taxpayer is resident in Canada and not exempt from tax under this Part on the taxpayer's taxable income.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

8. (1) Subparagraph 56(1)(*a*)(i) of the Act is amended by striking out the word "and" at the end of clause (D), by adding the word "and" at the end of clause (E) and by adding the following after clause (E):

(F) a benefit received under section 71 of the *Canada Pension Plan* or under a similar provision of a provincial pension plan as defined in section 3 of that Act,

(2) Subsection 56(1) of the Act is amended by adding the following after paragraph (*a*):

Benefits under CPP/QPP

(*a*.1) where the taxpayer is an estate that arose on or as a consequence of the death of an individual, each benefit received under section 71 of the *Canada Pension Plan*, or under a similar provision of a provincial pension plan as defined in section 3 of that Act, after ANNOUNCEMENT DATE and in the year in respect of the death of the individual;

(3) The portion of subsection 56(8) of the Act before paragraph (*b*) is replaced by the following:

CPP/QPP benefits for previous years

(8) Notwithstanding subsection (1), where

(*a*) one or more amounts are received by an individual (other than a trust) in a taxation year as, on account of, in lieu of payment of or in satisfaction of, any benefit under the *Canada Pension Plan* or a provincial pension plan as defined in section 3 of that Act, and

(4) Subsections (1) and (2) apply to the 1997 and subsequent taxation years except that clause 56(1)(*a*)(i)(F) of the Act, as enacted by subsection (1), does not apply to benefits received before ANNOUNCEMENT DATE + 1 by a taxpayer in respect of the death of an individual where the taxpayer is an estate that arose on or as a consequence of the death of the individual.

(5) Subsection (3) applies to amounts received after 1995.

9. (1) The English version of paragraph (*d*) of the definition "earned income" in subsection 63(3) of the Act is replaced by the following:

(*d*) all amounts received by the taxpayer as, on account of, in lieu of payment of or in satisfaction of, a disability pension under the *Canada Pension Plan* or a provincial plan as defined in section 3 of that Act;

(2) Subsection (1) applies to amounts received after 1995.

10. (1) The portion of section 64 of the Act before paragraph (*a*) is replaced by the following:

Attendant care expenses

64. Where a taxpayer in respect of whom an amount may be deducted because of section 118.3 for a taxation year files with the taxpayer's return of income (other than a return of income filed under subsection 70(2), paragraph 104(23)(*d*) or 128(2)(*e*) or subsection 150(4)) for the year a prescribed form containing prescribed information, there may be deducted in computing the taxpayer's income for the year the lesser of

(2) Section 64 of the Act is amended by adding the word "and" at the end of paragraph (*a*), by striking out the word "and" at the end of paragraph (*b*) and by repealing paragraph (*c*).

(3) Subsections (1) and (2) apply to the 1997 and subsequent taxation years.

11. (1) Paragraph 72(1)(*c*) of the Act is replaced by the following:

(*c*) no amount may be claimed under subparagraph 40(1)(*a*)(iii), paragraph 40(1.01)(*c*) or subparagraph 44(1)(*e*)(iii) in computing any gain of the taxpayer for the year;

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

12. (1) Paragraph 75(3)(*c*.1) of the Act is replaced by the following:

(*c*.1) by a qualifying environmental trust; or

(2) Subsection (1) applies to taxation years that end after February 22, 1994.

13. (1) Paragraphs 81(1)(*o*) and (*p*) of the Act are repealed.

(2) Subsection (1) applies to the 1998 and subsequent taxation years.

14. (1) Subsection 87(2) of the Act is amended by adding the following after paragraph (*m*):

Gift of non-qualifying security

(*m*.1) for the purpose of computing the new corporation's gain under subsection 40(1.01) for any taxation year from the disposition of a property, the new corporation is deemed to be the same corporation as, and a continuation of, each predecessor corporation;

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

15. (1) Subsection 88(1) of the Act is amended by adding the following after paragraph (*e*.6):

(*e*.61) the parent is deemed for the purpose of section 110.1 to have made any gift deemed by subsection 118.1(13) to have been made by the subsidiary after the subsidiary ceased to exist;

(2) Subsection (1) applies after ANNOUNCEMENT DATE.

16. (1) The definition "public corporation" in subsection 89(1) of the Act is replaced by the following:

"public corporation"
« société publique »

"public corporation" at any particular time means

(*a*) a corporation that is resident in Canada at the particular time if at that time a class of shares of the capital stock of the corporation is listed on a prescribed stock exchange in Canada,

(*b*) a corporation (other than a prescribed labour-sponsored venture capital corporation) that is resident in Canada at the particular time where at any time after June 18, 1971 and

(i) before the particular time, it elected in prescribed manner to be a public corporation, and at the time of the election it complied with prescribed conditions relating to the number of its shareholders, the dispersal of ownership of its shares and the public trading of its shares, or

(ii) before the day that is 30 days before the day that includes the particular time it was, by notice in writing to the corporation, designated by the Minister to be a public corporation and at the time it was so designated it complied with the conditions referred to in subparagraph (i),

unless after the election or designation, as the case may be, was made and before the particular time, it ceased to be a public corporation because of an election or designation under paragraph (*c*), or

(*c*) a corporation (other than a prescribed labour-sponsored venture capital corporation) that is resident in Canada at the particular time where, at any time after June 18, 1971 and before the particular time it was a public corporation, unless after the time it last became a public corporation and

(i) before the particular time, it elected in prescribed manner not to be a public corporation, and at the time it so elected it complied with prescribed conditions relating to the number of its shareholders, the dispersal of ownership of its shares and the public trading of its shares, or

(ii) before the day that is 30 days before the day that includes the particular time it was, by notice in writing to the corporation, designated by the Minister not to be a public corporation and at the time it was so designated it complied with the conditions referred to in subparagraph (i),

and where a corporation has, on or before its filing-due date for its first taxation year, become a public corporation, it is, if it so elects in its return of income for the year, deemed to have been a public corporation from the beginning of the year until the time at which it so became a public corporation;

(2) Subsection (1) applies to the 1995 and subsequent taxation years.

17. (1) The portion of subsection 107.3(1) of the Act before paragraph (*a*) is replaced by the following:

Treatment of beneficiaries under qualifying environmental trusts

107.3 (1) Where a taxpayer is a beneficiary under a qualifying environmental trust in a taxation year of the trust (in this subsection referred to as the "trust's year") that ends in a particular taxation year of the taxpayer,

(2) Paragraph 107.3(1)(*b*) of the Act is replaced by the following:

(*b*) where the taxpayer is non-resident at any time in the particular year and an income or loss described in paragraph (*a*) or an amount to which paragraph 12(1)(*z*.1) or (*z*.2) applies would not otherwise be included in computing the taxpayer's taxable income or taxable income earned in Canada, as the case may be, notwithstanding any other provision of this Act the income, the loss or the amount shall be attributed to the carrying on of business in Canada by the taxpayer through a fixed place of business located in the province in which the site to which the trust relates is situated.

(3) The portion of subsection 107.3(2) of the Act before paragraph (*a*) is replaced by the following:

Transfers to beneficiaries

(2) Where property of a qualifying environmental trust is transferred at any time to a beneficiary under the trust in satisfaction of all or any part of the beneficiary's interest as a beneficiary under the trust,

(4) The portion of subsection 107.3(3) of the Act before paragraph (*b*) is replaced by the following:

Ceasing to be a qualifying environmental trust

(3) Where a trust ceases at any time to be a qualifying environmental trust,

(*a*) the taxation year of the trust that would otherwise have included that time is deemed to have ended immediately before that time and a new taxation year of the trust is deemed to have begun at that time;

(5) Subsection 107.3(4) of the Act is replaced by the following:

Application

(4) Subsection 104(13) and sections 105 to 107 do not apply to a trust with respect to a taxation year during which it is a qualifying environmental trust.

(6) Subsections (1) to (5) apply to taxation years that end after February 18, 1997.

18. (1) The definition "preferred beneficiary" in subsection 108(1) of the Act is replaced by the following:

"preferred beneficiary"
« bénéficiaire privilégié »

"preferred beneficiary" under a trust for a particular taxation year of the trust means a beneficiary under the trust at the end of the particular year who is resident in Canada at that time where

(*a*) the beneficiary is

(i) an individual in respect of whom paragraphs 118.3(1)(*a*) to (*b*) apply for the individual's taxation year (in this definition referred to as the "beneficiary's year") that ends in the particular year, or

(ii) an individual

(A) who attained the age of 18 years before the end of the beneficiary's year, was a dependant (within the meaning assigned by subsection 118(6)) of another individual for the beneficiary's year and was dependent on the other individual because of mental or physical infirmity, and

(B) whose income (computed without reference to subsection 104(14)) for the beneficiary's year does not exceed $6,456, and

(*b*) the beneficiary is

(i) the settlor of the trust,

(ii) the spouse or former spouse of the settlor of the trust, or

(iii) a child, grandchild or great grandchild of the settlor of the trust or the spouse of any such person;

(2) Subsection (1) applies to trust taxation years that end after 1996.

19. (1) Subsection 110.1(1) of the Act is replaced by the following:

Deduction for gifts

110.1 (1) For the purpose of computing the taxable income of a corporation for a taxation year, there may be deducted such of the following amounts as the corporation claims:

Charitable gifts

(*a*) the total of all amounts each of which is the fair market value of a gift (other than a gift described in paragraph (*b*), (*c*) or (*d*)) made by the corporation in the year or in any of the 5 preceding taxation years to

(i) a registered charity,

(ii) a registered Canadian amateur athletic association,

(iii) a corporation resident in Canada and described in paragraph 149(1)(*i*),

(iv) a municipality in Canada,

(v) the United Nations or an agency thereof,

(vi) a university outside Canada that is prescribed to be a university the student body of which ordinarily includes students from Canada,

(vii) a charitable organization outside Canada to which Her Majesty in right of Canada has made a gift in the year or in the 12-month period preceding the year, or

(viii) Her Majesty in right of Canada or a province,

not exceeding the lesser of the corporation's income for the year and the amount determined by the formula

$$0.75A + 0.25 (B + C + D)$$

where

A is the corporation's income for the year computed without reference to subsection 137(2),

B is the total of all amounts each of which is a taxable capital gain of the corporation for the year from a disposition that is the

making of a gift made by the corporation in the year and described in this paragraph,

C is the total of all amounts each of which is a taxable capital gain of the corporation for the year from a disposition of a property because of subsection 40(1.01), and

D is the total of all amounts each of which is determined in respect of the corporation's depreciable property of a prescribed class and equal to the lesser of

(A) the amount included under subsection 13(1) in respect of the class in computing the corporation's income for the year, and

(B) the total of all amounts each of which is determined in respect of a disposition that is the making of a gift of property of the class by the corporation in the year that is described in this paragraph and equal to the lesser of

(I) the proceeds of disposition of the property minus any outlays and expenses to the extent that they were made or incurred by the corporation for the purpose of making the disposition, and

(II) the capital cost to the corporation of the property;

Gifts to Her Majesty

(*b*) the total of all amounts each of which is the fair market value of a gift (other than a gift described in paragraph (*c*) or (*d*)) made by the corporation to Her Majesty in right of Canada or a province

(i) in the year or in any of the 5 preceding taxation years, and

(ii) before February 19, 1997 or pursuant to a written agreement made before that day;

Gifts to institutions

(*c*) the total of all amounts each of which is the fair market value of a gift (other than a gift described in paragraph (*d*)) of an object that the Canadian Cultural Property Export Review Board has determined meets the criteria set out in paragraphs 29(3)(*b*) and (*c*) of the *Cultural Property Export and Import Act*, which gift was made by the corporation in the year or in any of the 5 preceding taxation years to an institution or a public authority in Canada that was, at the

time the gift was made, designated under subsection 32(2) of that Act either generally or for a specified purpose related to that object;

Ecological gifts

(*d*) the total of all amounts each of which is the fair market value of a gift of land, including a servitude for the use and benefit of a dominant land, a covenant or an easement, that is certified by the Minister of the Environment, or a person designated by that Minister, to be ecologically sensitive land, the conservation and protection of which is, in the opinion of that Minister, or that person, important to the preservation of Canada's environmental heritage, which gift was made by the corporation in the year or in any of the 5 preceding taxation years to

(i) Her Majesty in right of Canada or a province or a municipality in Canada, or

(ii) a registered charity one of the main purposes of which is, in the opinion of that Minister, the conservation and protection of Canada's environmental heritage, and that is approved by that Minister or that person in respect of the gift.

Limitation on deductibility

(1.1) For the purpose of determining the amount deductible under subsection (1) in computing a corporation's taxable income for a taxation year,

(*a*) an amount in respect of a gift is deductible only to the extent that it exceeds amounts in respect of the gift deducted under that subsection in computing the corporation's taxable income for preceding taxation years; and

(*b*) no amount in respect of a gift made in a particular taxation year is deductible under any of paragraphs (1)(*a*) to (*d*) until amounts deductible under that paragraph in respect of gifts made in taxation years preceding the particular year have been deducted.

(2) Section 110.1 of the Act is amended by adding the following after subsection (4):

Ecological gifts

(5) For the purpose of paragraph (1)(*d*), the fair market value of a gift of a servitude, a covenant or an easement to which land is subject is deemed to be the greater of its fair market value otherwise determined

and the amount by which the fair market value of the land is reduced as a consequence of the making of the gift.

Non-qualifying securities

(6) Subsections 118.1(13) and (15) to (18) apply to this section as if the references in those subsections to an individual were read as a corporation and as if a non-qualifying security of a corporation included a share (other than a share listed on a prescribed stock exchange) of the capital stock of the corporation.

Corporation ceasing to exist

(7) Where, but for this subsection, a corporation (other than a corporation that was a predecessor corporation in an amalgamation to which subsection 87(1) applied or a corporation that was wound up in a winding-up to which subsection 88(1) applied) would be deemed by subsection 118.1(13) to have made a gift after the corporation ceased to exist, for the purpose of this section, the corporation shall be deemed to have made the gift in its last taxation year, except that the amount of interest payable under any provision of this Act is the amount that it would be if this subsection did not apply to the gift.

(3) Subsection (1) applies to taxation years that begin after 1996.

(4) Subsection 110.1(5) of the Act, as enacted by subsection (2), applies to gifts made after February 27, 1995.

(5) Subsections 110.1(6) and (7) of the Act, as enacted by subsection (2), apply after ANNOUNCEMENT DATE.

20. (1) The portion of section 117.1(1) of the Act before paragraph (*c*) is replaced by the following:

Annual adjustment

117.1(1) Each of

(*a*) the amount of $6,456 referred to in clause (*a*)(ii)(B) of the definition "preferred beneficiary" in subsection 108(1) in relation to a beneficiary's income (computed without reference to subsection 104(14)) for a taxation year,

(*b*) the amounts expressed in dollars in subsection 117(2), paragraphs (*c*) and (*d*) of the description of B in subsection 118(1),

subsections 118(2), 118.2(1) and 118.3(1) and Part I.2 in relation to tax payable under this Part or Part I.2 for a taxation year,

(*b*.1) the amounts of $5,000 and $6,000 referred to in subsection (2) and paragraphs (*a*) and (*b*) of the description of B in subsection 118(1) in relation to tax payable under this Part for a taxation year, and

(*b*.2) the amounts expressed in dollars in subsections 122.5(3) and 122.51(1) and (2) in relation to tax payable under this Part for a taxation year

shall be adjusted so that the amount to be used under those provisions for the year is the total of

(2) Subsection (1) applies to the 1997 and subsequent taxation years, except that in applying paragraph 117.1(1)(*b*.2) of the Act, as enacted by subsection (1), to the 1997 taxation year the reference in that paragraph to "subsections 122.5(3) and 122.51(1) and (2)" shall be read as "subsection 122.5(3)".

(3) For the purpose of paragraph 117.1(1)(*c*) of the Act, the amount used under clause (*a*)(ii)(B) of the definition "preferred beneficiary" in subsection 108(1) of the Act, as enacted by subsection 18(1), in relation to income for the 1996 taxation year is deemed to be $6,456.

21. (1) The definition "total charitable gifts" in subsection 118.1(1) of the Act is amended by striking out the word "or" at the end of paragraph (*f*), by adding the word "or" at the end of paragraph (*g*) and by adding the following after paragraph (g):

(*g*.1) Her Majesty in right of Canada or a province,

(2) The definition "total Crown gifts" in subsection 118.1(1) of the Act is amending by striking out the word "and" at the end of paragraph (*a*), by adding the word "and" at the end of paragraph (*b*) and by adding the following after paragraph (*b*):

(*c*) in respect of gifts made before February 19, 1997 or pursuant to agreements in writing made before that day;

(3) Paragraph (*a*) of the definition "total ecological gifts" in subsection 118.1(1) of the Act is replaced by the following:

(*a*) Her Majesty in right of Canada or a province or a municipality in Canada, or

(4) Subparagraph (*a*)(iii) of the definition "total gifts" in subsection 118.1(1) of the Act is replaced by the following:

(iii) in any other case, the lesser of the individual's income for the year and the amount determined by the formula

$$0.75A + 0.25 (B + C + D - E)$$

where

A is the individual's income for the year,

B is the total of all amounts each of which is a taxable capital gain of the individual for the year from a disposition that is the making of a gift made by the individual in the year, which gift is included in the individual's total charitable gifts for the year,

C is the total of all amounts each of which is a taxable capital gain of the individual for the year from a disposition of a property because of subsection 40(1.01),

D is the total of all amounts each of which is determined in respect of the individual's depreciable property of a prescribed class and equal to the lesser of

(A) the amount included under subsection 13(1) in respect of the class in computing the individual's income for the year, and

(B) the total of all amounts each of which is determined in respect of a disposition that is the making of a gift of property of the class by the individual in the year that is included in the individual's total charitable gifts for the year and equal to the lesser of

(I) the proceeds of disposition of the property minus any outlays and expenses to the extent that they were made or incurred by the individual for the purpose of making the disposition, and

(II) the capital cost to the individual of the property, and

E is the total of all amounts each of which is the portion of an amount deducted under subsection 110.6 in computing the individual's taxable income for the year that can

reasonably be considered to be in respect of a gift referred to in the description of B,

(5) Section 118.1 of the Act is amended by adding the following after subsection (2):

Ordering

(2.1) For the purpose of determining the total charitable gifts, total Crown gifts, total cultural gifts and total ecological gifts of an individual for a taxation year, no amount in respect of a gift described in any of the definitions of those expressions and made in a particular taxation year shall be considered to have been included in determining an amount that was deducted under this section in computing the individual's tax payable under this Part for a taxation year until amounts in respect of such gifts made in taxation years preceding the particular year that can be so considered are so considered.

(6) Subsection 118.1(4) and (5) of the Act are replaced by the following:

Gift in year of death

(4) Subject to subsection (13), a gift made by an individual in the taxation year in which the individual dies (including, for greater certainty, a gift deemed by subsection (5) or (14) to have been so made) is deemed to have been made by the individual in the immediately preceding taxation year to the extent an amount in respect thereof is not deducted in computing the individual's tax payable under this Part for the taxation year in which the individual dies.

Gift by will

(5) Subject to subsection (13), where an individual by the individual's will makes a gift, the gift is, for the purpose of this section, deemed to have been made by the individual in the taxation year in which the individual died.

(7) Section 118.1 of the Act is amended by adding the following after subsection (11):

Ecological gifts

(12) For the purpose of the definition "total ecological gifts" in subsection (1), the fair market value of a gift of a servitude, a covenant or an easement to which land is subject is deemed to be the greater of its fair market value otherwise determined and the amount by which the

fair market value of the land is reduced as a result of the making of the gift.

Non-qualifying securities

(13) For the purpose of this section (other than this subsection), where at any particular time an individual makes a gift of a non-qualifying security of the individual,

(*a*) the gift is deemed not to have been made; and

(*b*) if the security is disposed of by the donee within 60 months after the particular time, the individual is deemed to have made a gift of property at the time of the disposition to the donee and the fair market value of that gift is deemed to be the lesser of the fair market value of any consideration (other than a non-qualifying security of the individual) received by the donee for the disposition and the fair market value of the gift made at the particular time.

Death of donor

(14) Where but for this subsection an individual would be deemed by subsection (13) to have made a gift after the individual's death, for the purpose of this section the individual is deemed to have made the gift in the taxation year in which the individual died, except that the amount of interest payable under any provision of this Act is the amount that it would be if this subsection did not apply to the gift.

Loanbacks

(15) For the purpose of this section, where

(*a*) at any particular time an individual makes a gift of property (other than a non-qualifying security of the individual), and

(*b*) within 60 months after the particular time

(i) the donee holds a non-qualifying security of the individual that was acquired by the donee after the time that is 60 months before the particular time, or

(ii) where the individual and the donee do not deal at arm's length with each other,

(A) the individual or any person or partnership with which the individual does not deal at arm's length uses property of the

donee pursuant to an agreement that was made or modified after the time that is 60 months before the particular time, and

(B) the property was not used in the carrying on of the donee's charitable activities,

the fair market value of the gift is deemed to be the amount otherwise determined minus the total of all amounts each of which is the fair market value of the consideration given by the donee to so acquire a non-qualifying security so held or the fair market value of such a property so used, as the case may be.

Ordering Rule

(16) For the purpose of applying subsection (15) to determine the fair market value of a gift made at any time, the fair market value of consideration given to acquire property described in subparagraph (15)(*b*)(i) or of property described in subparagraph (15)((*b*)(ii) is deemed to be that value otherwise determined minus any portion thereof that has been applied under that subsection to reduce the fair market value of another gift made before that time.

Non-qualifying security defined

(17) For the purposes of subsections (13) and (15), "non-qualifying security" of an individual at any time means

(*a*) an obligation (other than an obligation of a financial institution to repay an amount deposited with the institution or an obligation listed on a prescribed stock exchange) of the individual or of any person or partnership with which the individual does not deal at arm's length immediately after that time,

(*b*) a share (other than a share listed on a prescribed stock exchange) of the capital stock of a corporation with which the individual does not deal at arm's length immediately after that time, or

(*c*) any other security (other than a security listed on a prescribed stock exchange) issued by the individual or by any person or partnership with which the individual does not deal at arm's length immediately after that time.

Financial institution defined

(18) For the purpose of subsection (17), "financial institution" means a corporation that is

(*a*) a member of the Canadian Payments Association; or

(*b*) a credit union that is a shareholder or member of a body corporate or organization that is a central for the purposes of the *Canadian Payments Association Act*.

(8) Subsections (1), (2), (4) and (5) apply to taxation years that begin after 1996.

(9) Subsection (3) applies to gifts made after February 18, 1997.

(10) Subsection (6) and subsections 118.1(13) and (14) of the Act, as enacted by subsection (7), apply to gifts made after ANNOUNCEMENT DATE.

(11) Subsection 118.1(12) of the Act, as enacted by subsection (7), applies to gifts made after February 27, 1995.

(12) Subsection 118.1(15) of the Act, as enacted by subsection (7), applies where

(*a*) a non qualifying security referred to in subparagraph 118.1(15)(*b*)(i) of the Act, as enacted by subsection (7), is acquired after ANNOUNCEMENT DATE; or

(*b*) property referred to in subparagraph 118.1(15)(*b*)(ii) of the Act, as enacted by subsection (7), has begun to be used after ANNOUNCEMENT DATE.

(13) Subsections 118.1(16) to (18) of the Act, as enacted by subsection (7), apply after ANNOUNCEMENT DATE.

22. (1) The portion of paragraph 118.2(2)(*b*.1) of the Act after subparagraph (iv) is replaced by the following:

to the extent that the total of amounts so paid does not exceed $10,000 (or $20,000 where the individual dies in the year);

(2) Subsection 118.2(2) of the Act is amended by adding the following after paragraph (*l*.3):

(*l*.4) on behalf of the patient who has a speech or hearing impairment, for sign language interpretation services, to the extent that the payment is made to a person engaged in the business of providing such services;

(*l*.5) for reasonable moving expenses (within the meaning of subsection 62(3), but not including any expense deducted under

section 62 for any taxation year) of the patient, who lacks normal physical development or has a severe and prolonged mobility impairment, incurred for the purpose of the patient's move to a dwelling that is more accessible by the patient or in which the patient is more mobile or functional, where the total of the expenses claimed under this paragraph by all persons in respect of the move does not exceed $2,000;

(*l*.6) for reasonable expenses relating to alterations to the driveway of the principal place of residence of the patient who has a severe and prolonged mobility impairment, to facilitate the patient's access to a bus;

(*l*.7) for a van that, at the time of its acquisition or within 6 months after that time, has been adapted for the transportation of the patient who requires the use of a wheelchair, to the extent of the lesser of $5,000 and 20% of the amount by which

(i) the amount paid for the acquisition of the van

exceeds

(ii) the portion, if any, of the amount referred to in subparagraph (i), that is included because of paragraph (*m*) in computing the individual's deduction under this section for any taxation year;

(3) Paragraph 118.2(2)(*m*) of the Act is amended by adding the following after subparagraph (iv):

to the extent that the amount so paid does not exceed the amount, if any, prescribed in respect of the device or equipment;

(4) Subsections (1) to (3) apply to the 1997 and subsequent taxation years.

23. (1) Paragraph 118.3(1)(*a*.2) of the Act is replaced by the following:

(*a*.2) in the case of

(i) a sight impairment, a medical doctor or an optometrist,

(ii) a hearing impairment, a medical doctor or an audiologist, and

(iii) an impairment not referred to in subparagraph (i) or (ii), a medical doctor

has certified in prescribed form that the impairment is a severe and prolonged mental or physical impairment the effects of which are such that the individual's ability to perform a basic activity of daily living is markedly restricted,

(2) Subsection (1) applies to certifications made after February 18, 1997.

24. (1) The portion of subsection 118.4(2) of the Act before paragraph (*a*) is replaced by the following:

References to medical practitioners, etc.

(2) For the purposes of sections 63, 118.2 and 118.3, a reference to an audiologist, dentist, medical doctor, medical practitioner, nurse, optometrist or pharmacist is a reference to a person authorized to practice as such,

(2) Subsection (1) applies after February 18, 1997.

25. (1) Section 118.5 of the Act is amended by adding the following after subsection (2):

Inclusion of ancillary fees and charges

(3) For the purpose of this section, "fees for an individual's tuition" include ancillary fees and charges (other than fees and charges in respect of a student association) that are paid in respect of the individual's enrolment at a university, college or other educational institution in a program at a post-secondary school level, where the fee or charge is required to be paid to the institution by all of the institution's

(*a*) full-time students, where the individual is a full-time student at the institution, and

(*b*) part-time students, where the individual is a part-time student at the institution,

except to the extent that the fee or charge is levied in relation to

(*c*) property to be acquired by students,

(*d*) services not ordinarily provided at educational institutions in Canada that offer courses at a post-secondary school level,

(*e*) the provision of financial assistance to students, or

(*f*) the construction or renovation of any building or facility, except to the extent that the building or facility is owned by the institution and used to provide

(i) courses at the post-secondary school level, or

(ii) services for which, if fees or charges in respect thereof were required to be paid by all students of the institution, the fees or charges would be included because of this subsection in the fees for an individual's tuition.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

26. (1) The formula in subsection 118.6(2) of the Act is replaced by the following:

$$A \times \$\underline{200} \times B$$

(2) Subsection (1) applies to the 1997 and subsequent taxation years except that, for the 1997 taxation year, the reference to "$200" in the formula in subsection 118.6(2) of the Act, as enacted by subsection (1), shall be read as a reference to "$150".

27. (1) The Act is amended by adding the following after section 118.6:

Unused tuition and education tax credits

118.61 (1) In this section, an individual's unused tuition and education tax credits at the end of a taxation year is the amount determined by the formula

$$A + (B - C) - (D + E)$$

where

A is the individual's unused tuition and education tax credits at the end of the preceding taxation year;

B is the total of all amounts each of which may be deducted under section 118.5 or 118.6 in computing the individual's tax payable under this Part for the year;

C is the lesser of the value of B and the amount that would be the individual's tax payable under this Part for the year if no amount were deductible under section 118.5 or 118.6;

D is the amount that the individual may deduct under subsection (2) for the year; and

E is the tuition and education tax credits transferred for the year by the individual to the individual's spouse, parent or grandparent.

Deduction of carryforward

(2) For the purpose of computing an individual's tax payable under this Part for a taxation year, there may be deducted the lesser of

(*a*) the individual's unused tuition and education tax credits at the end of the preceding taxation year, and

(*b*) the amount that would be the individual's tax payable under this Part for the year if no amount were deductible under section 118.5 or 118.6 or this section.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

28. (1) The description of A in section 118.8 of the Act is replaced by the following:

A is the tuition and education tax credits transferred for the year by the spouse to the individual;

(2) The description of C in section 118.8 of the Act is replaced by the following:

C is the amount that would be the spouse's tax payable under this Part for the year if no amount were deductible under this Division (other than an amount deductible under subsection 118(1) because of paragraph (*c*) of the description of B in that subsection or under section 118.61 or 118.7).

(3) Subsections (1) and (2) apply to the 1997 and subsequent taxation years.

29. (1) The Act is amended by adding the following after section 118.8:

Tuition and education tax credits transferred

118.81 In this subdivision, the tuition and education tax credits transferred for a taxation year by a person to an individual is the least of

(*a*) the total of all amounts each of which may be deducted under section 118.5 or 118.6 in computing the person's tax payable under this Part for the year,

(*b*) the amount for the year that the person designates in writing for the purpose of section 118.8 or 118.9, and

(*c*) $850.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

30. (1) Section 118.9 of the Act is replaced by the following:

Transfer to parent or grandparent

118.9 Where for a taxation year a parent or grandparent of an individual (other than an individual in respect of whom the individual's spouse deducts an amount under section 118 or 118.8 for the year) is the only person designated in writing by the individual for the year for the purpose of this section, there may be deducted in computing the tax payable under this Part for the year by the parent or grandparent, as the case may be, the amount determined by the formula

A - B

where

A is the tuition and education tax credits transferred for the year by the individual to the parent or grandparent, as the case may be; and

B is the amount that would be the individual's tax payable under this Part for the year if no amount were deductible under this Division (other than an amount deductible under section 118, 118.3 or 118.7).

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

31. (1) Section 118.92 of the Act is replaced by the following:

Ordering of credits

118.92 In computing an individual's tax payable under this Part, the following provisions shall be applied in the following order: subsections 118(1) and (2), section 118.7, subsection 118(3) and sections 118.3, 118.61, 118.5, 118.6, 118.9, 118.8, 118.2, 118.1 and 121.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

32. (1) The Act is amended by adding the following after section 122.5:

Definitions

122.51 (1) The definitions in this subsection apply in this section.

"adjusted income"
« revenu modifié »

"adjusted income" of an individual for a taxation year has the meaning assigned for the purpose of subdivision a.1.

"eligible individual"
« particulier admissible »

"eligible individual" for a taxation year means an individual (other than a trust)

(*a*) who is resident in Canada throughout the year (or, where the individual dies in the year, throughout the portion of the year before the individual's death);

(*b*) who, before the end of the year, has attained the age of 18 years; and

(*c*) whose incomes for the year from all

(i) offices and employments (computed without reference to paragraph 6(1)(*f*)), and

(ii) businesses each of which is a business carried on by the individual either alone or as a partner actively engaged in the business

total $2,500 or more.

Deemed payment on account of tax

(2) Where a return of income (other than a return of income filed under subsection 70(2), paragraph 104(23)(*d*) or 128(2)(*e*) or subsection 150(4)) is filed in respect of an eligible individual for a particular taxation year that ends at the end of a calendar year, there is deemed to be paid at the end of the particular year on account of the individual's tax payable under this Part for the particular year the amount determined by the formula

A - B

where

A is the lesser of

(*a*) $500, and

(*b*) 25/17 of the total of all amounts deducted under subsection 118.2(1) in computing the individual's tax payable under this Part for all taxation years that end in the calendar year; and

B is 5% of the amount, if any, by which

(*a*) the individual's adjusted income for the particular year

exceeds

(*b*) $16,069.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

33. (1) The portion of the definition "investment tax credit" in subsection 127(9) of the Act after paragraph (*k*) is replaced by the following:

except that no amount shall be included in the total determined under any of paragraphs (*a*) to (*e*.2) in respect of an outlay, expense or expenditure that would, if this Act were read without reference to subsections (26) and 78(4), be made or incurred by the taxpayer in the course of earning income in a particular taxation year, and no amount shall be added under paragraph (*b*) in computing the taxpayer's investment tax credit at the end of a particular taxation year in respect of an outlay, expense or expenditure made or incurred by a trust or a partnership in the course of earning income, if

(*l*) any of the income is exempt income, or

(*m*) the taxpayer does not file with the Minister a prescribed form containing prescribed information in respect of the amount on or before the day that is one year after the taxpayer's filing-due date for the particular year;

(2) Paragraphs (*e*) to (*g*) of the definition "qualified expenditure" in subsection 127(9) of the Act are replaced by the following:

(*f*) an expenditure (other than an expenditure that is salary or wages of an employee of the taxpayer) incurred by the taxpayer in respect of scientific research and experimental development to the extent that it is performed by another person or partnership at a time when the taxpayer and the person or partnership to which the expenditure is paid or payable do not deal with each other at arm's length,

(*g*) an expenditure described in paragraph 37(1)(*a*) that is paid or payable by the taxpayer to or for the benefit of a person or partnership that is not a taxable supplier in respect of the expenditure, other than an expenditure in respect of scientific research and experimental development directly undertaken by the taxpayer, and

(3) That portion of the definition "taxable supplier" in subsection 127(9) after paragraph (a) is replaced by the following:

(*b*) a non-resident person, or a partnership that is not a Canadian partnership,

(i) by which the amount was payable, or

(ii) by or for whom the amount was receivable

in the course of carrying on a business through a permanent establishment (as defined by regulation) in Canada.

(4) Subsection 127(11.4) is replaced by the following:

Reclassified expenditures

(11.4) Paragraph (*m*) of the definition "investment tax credit" in subsection (9) does not apply to an expenditure incurred in a taxation year by a taxpayer where the expenditure is reclassified by the Minister on an assessment of the taxpayer's tax payable under this Part for the year, or on a determination that no tax under this Part is payable for the

year by the taxpayer, as an expenditure in respect of scientific research and experimental development.

(5) Subsection 127(11.4) is repealed.

(6) Subsection (1) applies to all taxation years, except that where the taxpayer's filing-due date for the year is before June 1996, the taxpayer may file the prescribed form referred to in paragraph (*m*) of the definition "investment tax credit" in subsection 127(9) of the Act, as enacted by subsection (1), before June 1997, and, for the purposes of this subsection and subsection (1), the definition "filing-due date" in subsection 248(1) of the Act applies to all taxation years.

(7) Subsections (2) and (3) apply to taxation years that begin after 1995.

(8) Subsection (4) applies to the 1996 taxation year.

(9) Subsection (5) applies to the 1997 and subsequent taxation years.

34. (1) The description of A in paragraph 127.41(1)(*a*) of the Act is replaced by the following:

A is the tax payable under Part XII.4 by a qualifying environmental trust for a taxation year (in this paragraph referred to as the "trust's year") that ends in the particular year,

(2) Subsection (1) applies to taxation years that end after February 18, 1997.

35. (1) Subparagraph 127.52(1)(*d*)(i) of the Act is replaced by the following:

(i) sections 38 and 41 were read without the references therein to "3/4 of", other than in the case of a capital gain from a disposition that is the making of a gift of property to a qualified donee (as defined in subsection 149.1(1)), and

(2) Subsection (1) applies to taxation years that begin after 1996.

36. (1) Paragraph 128(2)(*f*) of the Act is amended by striking out the word "and" at the end of subparagraph (ii), by adding the word "and" at the end of subparagraph (iii) and by adding the following after subparagraph (iii):

(iv) in computing the individual's tax payable under this Part for the year, no amount were deductible under section 118.61,

(2) Paragraph 128(2)(*g*) of the Act is replaced by the following:

(*g*) notwithstanding subparagraphs (*e*)(ii) and (iii) and (*f*)(iii) and (iv), where at any time an individual was discharged absolutely from bankruptcy,

(i) in computing the individual's taxable income for any taxation year that ends after that time, no amount shall be deducted under section 111 in respect of losses for taxation years that ended before that time, and

(ii) the individual's unused tuition and education tax credits at the end of the last taxation year that ended before that time is deemed to be nil;

(3) Subsections (1) and (2) apply to the 1997 and subsequent taxation years.

37. (1) Subparagraph 128.1(4)(*b*)(iii) of the Act is replaced by the following:

(iii) where the taxpayer is an individual, a right to receive a payment described in any of paragraphs 212(1)(*h*) and (*j*) to (*q*), a right under a registered education savings plan or a right to receive any payment of a benefit under the *Canada Pension Plan* or a provincial pension plan as defined in section 3 of that Act,

(2) Subsection (1) applies after 1997.

38. (1) The English version of paragraph (*b*.1) of the definition "earned income" in subsection 146(1) of the Act is replaced by the following:

(*b*.1) an amount received by the taxpayer in the year and at a time when the taxpayer is resident in Canada as, on account of, in lieu of payment of or in satisfaction of, a disability pension under the *Canada Pension Plan* or a provincial plan as defined in section 3 of that Act,

(2) The formula in the definition "RRSP deduction limit" in subsection 146(1) of the Act is replaced by the following:

$$A + B + R - C$$

(3) The definition "RRSP deduction limit" in subsection 146(1) of the Act is amended by striking out the word "and" at the end of the description of B, by adding the word "and" at the end of the description of C and by adding the following after the description of C:

R is the taxpayer's total pension adjustment reversal for the year;

(4) The formula in paragraph (*b*) of the definition "unused RRSP deduction room" in subsection 146(1) of the Act is replaced by the following:

$$A + B + R - (C + D)$$

(5) Paragraph (*b*) of the definition "unused RRSP deduction room" in subsection 146(1) of the Act is amended by striking out the word "and" at the end of the description of C, by adding the word "and" at the end of the description of D and by adding the following after the description of D:

R is the taxpayer's total pension adjustment reversal for the year.

(6) Subsection (1) applies to amounts received after 1995.

(7) Subsections (2) to (5) apply to the 1998 and subsequent taxation years.

39. (1) The definitions "pre-1972 income" and "tax-paid-income" in subsection 146.1(1) of the Act are repealed.

(2) The definitions "educational assistance payment", "education savings plan", "refund of payments" and "registered education savings plan" in subsection 146.1(1) of the Act are replaced by the following:

"educational assistance payment"

« paiement d'aide aux études »

"educational assistance payment" means any amount, other than a refund of payments, paid out of an education savings plan to or for an

individual to assist the individual to further the individual's education at a post-secondary school level;

"education savings plan"
« régime d'épargne-études »

"education savings plan" means a contract made at any time between

(*a*) either

(i) one individual (other than a trust), or

(ii) an individual (other than a trust) and the spouse of the individual, and

(*b*) a person or organization (in this section referred to as a "promoter")

under which the promoter agrees to pay or to cause to be paid educational assistance payments to or for one or more beneficiaries;

"refund of payments"
« remboursement de paiements »

"refund of payments" at any time under a particular registered education savings plan means

(*a*) a refund at that time of a contribution that had been made at a previous time, where the contribution was made

(i) otherwise than by way of a transfer from another registered education savings plan, and

(ii) into the particular plan by or on behalf of a subscriber under the particular plan, or

(*b*) a refund at that time of an amount that was paid at a previous time into the particular plan by way of a transfer from another registered education savings plan, where the amount would have been a refund of payments under the other plan if it had been paid at the previous time directly to a subscriber under the other plan;

"registered education savings plan"
« régime enregistré d'épargne-études »

"registered education savings plan" means

(*a*) an education savings plan registered for the purposes of this Act, or

(*b*) a registered education savings plan as it is amended from time to time

but, except for the purposes of subsections (7) and (7.1) and Part X.4, a plan shall cease to be a registered education savings plan immediately after the day as of which its registration is revoked under subsection (13);

(3) The portion of the definition "trust" in subsection 146.1(1) of the Act before paragraph (*c*) is replaced by the following:

"trust"
« fiducie »

"trust", except in this definition and the definition "education savings plan", means any person who irrevocably holds property under an education savings plan for any of, or any combination of, the following purposes:

(*a*) the payment of educational assistance payments,

(*b*) the payment after 1997 of accumulated income payments,

(4) Subsection 146.1(1) of the Act is amended by adding the following definitions in alphabetical order:

"accumulated income payment"
« paiement de revenu accumulé »

"accumulated income payment" under an education savings plan means any amount paid out of the plan, other than a payment described in any of paragraphs (*a*), (*c*), (*d*) and (*e*) of the definition "trust", to the extent that the amount so paid exceeds the fair market value of any consideration given to the plan for the payment of the amount;

"RESP annual limit"
« plafond annuel de REEE »

"RESP annual limit" for a year means

(*a*) for the 1990 to 1995 years, $1,500,

(*b*) for the 1996 year, $2,000, and

(*c*) for the 1997 and subsequent years, $4,000;

"subscriber"
« souscripteur »

"subscriber" under an education savings plan at any time means

(*a*) each individual with whom the promoter of the plan entered into the plan,

(*b*) an individual who has before that time acquired a subscriber's rights under the plan pursuant to a decree, order or judgment of a competent tribunal or under a written agreement, relating to a division of property between the individual and a subscriber under the plan in settlement of rights arising out of, or on the breakdown of, their marriage, or

(*c*) after the death of a subscriber under the plan, any other person (including the estate of the subscriber) who makes contributions into the plan in respect of a beneficiary

but does not include an individual who, before that time, disposed of the individual's rights as a subscriber under the plan in the circumstances described in paragraph (*b*);

(5) The portion of subsection 146.1(2) of the Act before paragraph (*a*) is replaced by the following:

Conditions for registration

(2) The Minister shall not accept for registration for the purposes of this Act any education savings plan of a promoter unless, in the Minister's opinion, the following conditions are complied with:

(6) Paragraph 146.1(2)(*b*) of the Act is replaced by the following:

(*b*) at the time of the application by the promoter for registration of the plan, there are not fewer than 150 plans entered into with the promoter each of which complied, at the time it was entered into, with all the other conditions set out in this subsection, as it read at that time;

(7) Paragraph 146.1(2)(*d*) of the Act is replaced by the following:

(*d*) the plan does not allow for any payment before 1998 to a subscriber, other than a refund of payments, unless the subscriber is also the beneficiary under the plan;

(*d*.1) the plan does not allow accumulated income payments under the plan or the plan allows an accumulated income payment at a particular time under the plan only where

(i) the payment is made to, or on behalf of, a person and not jointly to, or on behalf of, more than one person,

(ii) the particular time is after 1997,

(iii) the person is resident in Canada at the particular time,

(iv) either

(A) the person is a subscriber under the plan at the particular time, or

(B) an individual died at any previous time and was a subscriber under the plan immediately before death,

(v) each individual in respect of whom a subscriber has made a contribution into the plan,

(A) has before the particular time attained 21 years of age and is not, at the particular time, eligible under the plan to receive an educational assistance payment, or

(B) has died before the particular time, and

(vi) either

(A) the particular time is after the 9th year that follows the year in which the plan was entered into, or

(B) each individual in respect of whom a subscriber has made a contribution into the plan has died before the particular time and was, or was related to, a subscriber under the plan (or was

the nephew, niece, great nephew or great niece of a subscriber under the plan);

(8) Paragraph 146.1(2)(*g*) of the Act is replaced by the following:

(*g*) the plan does not allow for the payment of educational assistance payments before 1997 to an individual unless the individual is, at the time the payment is made, a student in full-time attendance at a post-secondary educational institution and enrolled in a qualifying educational program at the institution;

(*g*.1) the plan does not allow for the payment of educational assistance payments after 1996 to an individual unless the individual is, at the time the payment is made, enrolled in a qualifying educational program as a full-time student at a post-secondary educational institution;

(*g*.2) the plan does not allow for any contribution into the plan, other than a contribution made by or on behalf of a subscriber under the plan in respect of a beneficiary under the plan or a contribution made by way of transfer from another registered education savings plan;

(9) Subsection 146.1(2) of the Act is amended by adding the following after paragraph (*i*):

(*i*.1) where the plan allows accumulated income payments in accordance with paragraph (*d*.1), the plan provides that it must be terminated before March of the year following the year in which the first such payment is made out of the plan;

(*i*.2) the plan does not allow for the receipt of property by way of direct transfer from another registered education savings plan after the other plan has made any accumulated income payment;

(10) Paragraph 146.1(2)(*j*) of the Act is replaced by the following:

(*j*) where the plan allows more than one beneficiary under the plan at any one time, the plan provides

(i) that each of the beneficiaries under the plan is required to be connected to each living subscriber under the plan, or to have been connected to a deceased original subscriber under the plan, by blood relationship or adoption, and

(ii) that a contribution into the plan in respect of a beneficiary is permitted to be made only if

(A) the beneficiary had not attained 21 years of age at the time the plan was entered into,

(B) the contribution is made by way of transfer from another registered education savings plan into which a contribution had been made before the transfer in respect of the beneficiary, or

(C) the contribution is made after a contribution, to which clause (B) applies, into the plan in respect of the beneficiary;

(11) Paragraph 146.1(2)(*k*) of the Act is replaced by the following:

(*k*) the plan does not allow the total of all contributions made into the plan in respect of a beneficiary for a year (other than contributions made by way of transfer from registered education savings plans) to exceed the RESP annual limit for the year;

(12) Paragraph 146.1(2)(*m*) of the Act is replaced by the following:

(*m*) the Minister has no reasonable basis to believe that the promoter will not take all reasonable measures to ensure that the plan will continue to comply with the conditions in paragraphs (*a*), (*c*) to (*d*.1) and (*f*) to (*l*) for its registration for the purposes of this Act.

(13) Section 146.1 of the Act is amended by adding the following after subsection (4):

Obligation to file amendment

(4.1) Where a registered education savings plan is amended, the promoter shall file the text of the amendment with the Minister not later than 60 days after the day on which the plan is amended.

(14) Paragraph 146.1(6.1)(*a*) of the Act is repealed.

(15) Paragraph 146.1(6.1)(*b*) of the Act is replaced by the following:

(*b*) for the purposes of this paragraph, subparagraph (2)(*d*.1)(vi) and paragraphs (2)(*h*) and (*i*), the transferee plan is deemed to have been entered into on the day that is the earlier of

(i) the day on which the transferee plan was entered into, and

(ii) the day on which the transferor plan was entered into; and

(c) notwithstanding subsections (7) and (7.1), no amount shall be included in computing the income of any person because of the transfer.

(16) Subsection 146.1(7) of the Act is replaced by the following:

Educational assistance payments

(7) There shall be included in computing an individual's income for a taxation year the total of all educational assistance payments paid out of a registered education savings plan to or for the individual in the year.

Other income inclusions

(7.1) There shall be included in computing a taxpayer's income for a taxation year

(*a*) each accumulated income payment received in the year by the taxpayer under a registered education savings plan; and

(*b*) each amount received in the year by the taxpayer in full or partial satisfaction of a subscriber's interest under a registered education savings plan (other than any excluded amount in respect of the plan).

Excluded amount

(7.2) For the purpose of paragraph (7.1)(*b*), an excluded amount in respect of a registered education savings plan means

(*a*) any amount received under the plan;

(*b*) any amount received in satisfaction of a right to a refund of payments under the plan; or

(*c*) any amount received by a taxpayer under a decree, order or judgment of a competent tribunal or under a written agreement, relating to a division of property between the taxpayer and the taxpayer's spouse or former spouse in settlement of rights arising out of, or on the breakdown of, their marriage.

(17) Subsections 146.1(8) to (10) of the Act are repealed.

(18) Subsection 146.1(13) of the Act is replaced by the following:

Notice of intent to revoke registration

(12.1) Where a particular day is

(*a*) a day on which a registered education savings plan ceases to comply with the conditions of subsection (2) for the plan's registration,

(*b*) a day on which a registered education savings plan ceases to comply with any provision of the plan, or

(*c*) the last day of a month in respect of which tax is payable under Part X.4 by an individual because of contributions made, or deemed for the purpose of Part X.4 to have been made, by or on behalf of the individual into a registered education savings plan,

the Minister may send written notice (referred to in this subsection and subsection (12.2) as a "notice of intent") to the promoter of the plan that the Minister proposes to revoke the registration of the plan as of the day specified in the notice of intent, which day shall not be earlier than the particular day.

Notice of revocation

(12.2) Where the Minister sends a notice of intent to revoke the registration of a registered education savings plan to the promoter of the plan, the Minister may, after 30 days after the receipt by the promoter of the notice, send written notice (referred to in this subsection and subsection (13) as a "notice of revocation") to the promoter that the registration of the plan is revoked as of the day specified in the notice of revocation, which day shall not be earlier than the day specified in the notice of intent.

Revocation of registration

(13) Where the Minister sends a notice of revocation of the registration of a registered education savings plan under subsection (12.2) to the promoter of the plan, the registration of the plan is revoked as of the day specified in the notice of revocation, unless the Federal Court of Appeal or a judge thereof, on application made at any time before the determination of an appeal under subsection 172(3), orders otherwise.

(19) Subsection 146.1(14) of the Act is repealed.

(20) Section 146.1 of the Act is amended by adding the following:

Regulations

(15) The Governor in Council may make regulations requiring promoters of education savings plans to file information returns in respect of such plans.

(21) Subsection (1), the definitions "educational assistance payment" and "registered education savings plan" in subsection 146.1(1) of the Act, as enacted by subsection (2), subsection (3), the definition "accumulated income payment" in subsection 146.1(1) of the Act, as enacted by subsection (4), paragraph 146.1(6.1)(*b*) of the Act, as enacted by subsection (15), and subsections (18) and (19) apply after 1997.

(22) The definition "education savings plan" in subsection 146.1(1) of the Act, as enacted by subsection (2), and the definition "subscriber" in subsection 146.1(1) of the Act, as enacted by subsection (4), apply to contracts made after 1997.

(23) The definition "refund of payments" in subsection 146.1(1) of the Act, as enacted by subsection (2), and paragraph 146.1(2)(*g*.2) of the Act, as enacted by subsection (8), apply to the 1997 and subsequent taxation years.

(24) The definition "RESP annual limit" in subsection 146.1(1) of the Act, as enacted by subsection (4), applies after 1989.

(25) Subsections (5), (6) and (12) apply to applications made after 1997.

(26) Subsections (7), (9), (10), (16) and (17) apply to the 1998 and subsequent taxation years, except that

(*a*) paragraph 146.1(2)(*j*) of the Act, as enacted by subsection (10), does not apply to plans entered into before July 14, 1990; and

(*b*) subparagraph 146.1(2)(*j*)(ii) of the Act, as enacted by subsection (10), does not apply to plans entered into before 1998.

(27) Paragraphs 146.1(2)(*g*) and (*g*.1) of the Act, as enacted by subsection (8), apply to plans entered into after February 20, 1990, except that for plans entered into before 1998 the reference to "an individual" in the latter paragraph shall be read as "a beneficiary" and the reference to "the individual" in the latter paragraph shall be read as "the beneficiary".

(28) Subsection (11) applies to plans entered into after February 20, 1990.

(29) Subsection (14) applies to transfers made after 1996.

(30) Paragraph 146.1(6.1)(*c*) of the Act, as enacted by subsection (15), applies to transfers made after 1997.

40. (1) Paragraph 147.1(18)(*d*) of the Act is replaced by the following:

(*d*) requiring administrators of registered pension plans to make determinations in connection with the computation of pension adjustments, past service pension adjustments, pension adjustment reversals or any other related amounts (all such amounts referred to in this subsection as "specified amounts");

(2) Paragraph 147.1(18)(*t*) of the Act is replaced by the following:

(*t*) defining, for the purposes of this Act, the expressions "multi-employer plan", "past service event", "past service pension adjustment", "pension adjustment", "specified multi-employer plan" and "total pension adjustment reversal"; and

(3) Subsections (1) and (2) apply after 1996.

41. (1) Section 147.3 of the Act is amended by adding the following after subsection (14):

Transfer of property between provisions

(14.1) Where property held in connection with a benefit provision of a registered pension plan is made available to pay benefits under another benefit provision of the plan, subsections (9) to (11) apply in respect of the transaction by which the property is made so available in the same manner as they would apply if the other benefit provision were in another registered pension plan.

(2) Subsection (1) applies to transactions that occur on or after ANNOUNCEMENT DATE.

42. (1) Paragraph 149(1)(*z*) of the Act is replaced by the following:

Qualifying environmental trust

(*z*) a qualifying environmental trust.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

43. (1) Paragraph 152(1)(*b*) of the Act is replaced by the following:

(*b*) the amount of tax, if any, deemed by subsection 120(2), 122.5(3), 122.51(2), 125.4(3), 127.1(1), 127.41(3) or 210.2(3) or (4) to be paid on account of the taxpayer's tax payable under this Part for the year.

(2) Paragraph 152(4)(*b*) of the Act is amended by striking out the word "or" at the end of subparagraph (iii), by adding the word "or" at the end of subparagraph (iv) and by adding the following after subparagraph (iv):

(v) is made in order to give effect to the application of subsection 118.1(14) or (15).

(3) Paragraph 152(4.01)(*b*) of the Act is amended by striking out the word "or" at the end of subparagraph (iii), by adding the word "or" at the end of subparagraph (iv) and by adding the following after subparagraph (iv):

(v) the application referred to in subparagraph (4)(*b*)(v).

(4) Paragraph 152(4.2)(*d*) of the Act is replaced by the following:

(*d*) redetermine the amount, if any, deemed by subsection 120(2), 122.5(3), 122.51(2), 127.1(1), 127.41(3) or 210.2(3) or (4) to be paid on account of the taxpayer's tax payable under this Part for the year or deemed by subsection 122.61(1) to be an overpayment on account of the taxpayer's liability under this Part for the year.

(5) Subsections (1) and (4) apply to the 1997 and subsequent taxation years except that, for the 1997 taxation year, the references to "subsection 120(2)," in paragraphs 152(1)(*b*) and (4.2)(*d*) of the Act, as enacted by subsections (1) and (3), respectively, shall be read as references to "subsection 120(2), 120.1(4),".

(6) Subsections (2) and (3) apply after ANNOUNCEMENT DATE.

44. (1) Subsection 153(1) of the Act is amended by striking out the word "or" at the end of paragraph (*q*), by adding the word "or" at the end of paragraph (*r*) and by the following after paragraph (*r*):

(*s*) a payment made under a plan that was a registered education savings plan

(2) Subsection (1) applies to payments made after 1997.

45. (1) The description of A in paragraph (*b*) of the definition "net tax owing" in subsection 156.1(1) of the Act is replaced by the following:

A is the total of the taxes payable under this Part and Parts I.1, I.2 and X.5 by the individual for the year,

(2) Subsection (1) applies to the 1998 and subsequent taxation years.

46. (1) Paragraph 163(2)(*c*.2) of the Act is replaced by the following:

(*c*.2) the amount, if any, by which

(i) the amount that would be deemed under subsection 122.51(2) to be paid on account of the person's tax payable under this Part for the year if the amount were calculated by reference to the information provided in the return

exceeds

(ii) the amount that is deemed under subsection 122.51(2) to be paid on account of the person's tax payable under this Part for the year,

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

47. (1) Paragraph 172(3)(*e*) of the Act is replaced by the following:

(*e*) refuses to accept for registration for the purposes of this Act an education savings plan,

(*e*.1) sends notice under subsection 146.1(12.1) to a promoter that the Minister proposes to revoke the registration of an education savings plan,

(2) The portion of subsection 172(3) of the Act after paragraph (*g*) is replaced by the following:

the applicant or the organization, foundation, association or registered charity, as the case may be, in a case described in paragraph (*a*) or (*a*.1), the applicant in a case described in paragraph (*b*), (*d*), (*e*) or (*g*), a trustee under the plan or an employer of employees who are beneficiaries under the plan, in a case described in paragraph (*c*), the promoter in a case described in paragraph (*e*.1), or the administrator of the plan or an employer who participates in the plan, in a case described in paragraph (*f*) or (*f*.1), may appeal from the Minister's decision, or from the giving of the notice by the Minister, to the Federal Court of Appeal.

(3) Subsections (1) and (2) apply after 1997.

48. (1) Subsection 180(1) of the Act is amended by striking out the word "or" at the end of paragraph (*c*) and by adding the following after paragraph (*c*):

(*c*.1) the sending of a notice to a promoter of a registered education savings plan under subsection 146.1(12.1), or

(2) Subsection (1) applies after 1997.

49. (1) The description of C in subsection 190.1(1.2) of the Act is replaced by the following:

C is the number of days in the year that are after February 27, 1995 and before November 1998.

(2) Subsection (1) applies to taxation years that end after February 27, 1995.

50. (1) The formula in paragraph 204.2(1.1)(*b*) of the Act is replaced by the following:

$$A + B + R + C + D + E$$

(2) Paragraph 204.2(1.1)(*b*) of the Act is amended by striking out the word "and" at the end of the description of D, by adding the word "and" at the end of the description of E and by adding the following after the description of E:

R is the individual's total pension adjustment reversal for the year.

(3) Subsections (1) and (2) apply to the 1998 and subsequent taxation years.

51. (1) The heading "REGISTERED LABOUR-SPONSORED VdsENTURE CAPITAL CORPORATIONS" before section 204.8 of the Act is replaced by the following:

LABOUR-SPONSORED VENTURE CAPITAL CORPORATIONS

(2) Subsection (1) applies after February 18, 1997.

52. (1) The portion of the definition "eligible investment" in section 204.8 of the Act after paragraph (*d*) is replaced by the following:

if the following conditions are satisfied:

(*e*) immediately after the time the share or debt obligation was issued, the guarantee was provided or the option or right was granted, as the case may be, the total of the costs to the particular corporation of all shares, options, rights and debt obligations of the eligible business entity and all corporations related to it and 25% of the amount of all guarantees provided by the particular corporation in respect of debt obligations of the eligible business entity and the related corporations does not exceed the lesser of $15,000,000 and 10% of the shareholders' equity in the particular corporation, determined in accordance with generally accepted accounting principles, on a cost basis and without taking into account any unrealized gains or losses on the investments of the particular corporation, and

(*f*) immediately before the time the share or debt obligation was issued, the guarantee was provided or the option or right was granted, as the case may be,

(i) the carrying value of the total assets of the eligible business entity and all corporations (other than prescribed labour-sponsored venture capital corporations) related to it (determined in accordance with generally accepted accounting principles on a consolidated or combined basis, where applicable) did not exceed $50,000,000, and

(ii) the total of

(A) the number of employees of the eligible business entity and all corporations related to it who normally work at least 20 hours per week for the entity and the related corporations, and

(B) 1/2 of the number of other employees of the entity and the related corporations,

did not exceed 500;

(2) Subsection (1) applies to property acquired after February 18, 1997.

53. (1) Clause 204.81(1)(*c*)(ii)(C) of the Act is replaced by the following:

(C) such additional classes of shares as are authorized, where the rights, privileges, restrictions and conditions attached to the shares are approved by the Minister of Finance,

(2) Subsection (1) applies after 1996.

54. (1) Subsection 204.82(2) of the Act is replaced by the following:

Liability for tax

(2) Each corporation that has been registered under this Part shall, in respect of each month that ends in a particular taxation year of the corporation that begins after the end of the corporation's last taxation year referred to in paragraph 204.81(6)(*g*), pay a tax under this Part equal to the amount obtained when the greatest investment shortfall at any time that is in the month and in the particular year (in this section and sections 204.81 and 204.83 referred to as the "monthly deficiency") is multiplied by 1/60 of the prescribed rate of interest during the month.

Determination of investment shortfall

(2.1) Subject to subsection (2.2), a corporation's investment shortfall at any time in a particular taxation year is the amount determined by the formula

A - B

where

A is 60% of the lesser of

(*a*) the amount of the shareholders' equity in the corporation at the end of the preceding taxation year, and

(*b*) the amount of the shareholders' equity in the corporation at the end of the particular year; and

B is the greater of

(*a*) the total of all amounts each of which is the adjusted cost to the corporation of an eligible investment of the corporation at that time, and

(*b*) 50% of the total of all amounts each of which is

(i) the adjusted cost to the corporation of an eligible investment of the corporation at the beginning of the particular year, or

(ii) the adjusted cost to the corporation of an eligible investment of the corporation at the end of the particular year.

Investment shortfall

(2.2) For the purpose of computing a corporation's investment shortfall under subsection (2.1) at any time in a taxation year (in this subsection referred to as the "relevant year"),

(*a*) unrealized gains and losses in respect of its eligible investments shall not be taken into account in computing the amount of the shareholders' equity in the corporation;

(*b*) where

(i) the relevant year ends after 1998, and

(ii) it is expected that a redemption of its Class A shares will occur after the end of a particular taxation year and, as a consequence, the amount of the shareholders' equity in the corporation at the end of the particular year would otherwise be reduced to take into account the expected redemption,

subject to paragraph (*c*), the amount (or, where the relevant year ends in 1999, 2000, 2001 or 2002, 20%, 40%, 60% or 80%, as the case may be, of the amount) expected to be redeemed shall not be taken into account in determining the amount of the shareholders' equity in the corporation at the end of the particular year;

(*c*) paragraph (*b*) does not apply to a redemption expected to be made after the end of a taxation year where

(i) the redemption is made within 60 days after the end of the year, and

(ii) either

(A) tax under Part XII.5 became payable as a consequence of the redemption, or

(B) tax under Part XII.5 would not have become payable as a consequence of the redemption if the redemption had occurred at the end of the year; and

(*d*) the adjusted cost to the corporation of an eligible investment of the corporation at any time is

(i) where the eligible investment is a property acquired by the corporation after February 18, 1997 that would be an eligible investment of the corporation if the reference to "$50,000,000" in paragraph (*f*) of the definition "eligible investment" in section 204.8 were read as "$10,000,000", 150% of the cost to the corporation of the eligible investment of the corporation at that time, and

(ii) in any other case, the cost to the corporation of the eligible investment of the corporation at that time.

(2) Section 204.82 of the Act is amended by adding the following after subsection (4):

Provincially-registered LSVCCs

(5) Where

(*a*) an amount (other than interest on an amount to which this subsection applies or an amount payable under or as a consequence of a prescribed provision of a law of a province) is payable to the government of a province by a corporation,

(*b*) the amount is payable as a consequence of a failure to acquire sufficient properties of a character described in the law of the province,

(*c*) the corporation has been prescribed for the purpose of the definition "approved share" in subsection 127.4(1), and

(*d*) the corporation is not a registered labour-sponsored venture capital corporation or a revoked corporation,

the corporation shall pay a tax under this Part for the taxation year in which the amount became payable equal to that amount.

(3) Subsection (1) applies to taxation years that end after February 1997 except that, for taxation years that end before 1999, the amount determined under paragraph (*b*) of the description of B in subsection 204.82(2.1) of the Act, as enacted by subsection (1), is deemed to be nil.

(4) Subsection (2) applies to liabilities arising after February 18, 1997.

55. (1) Section 204.83 of the Act is replaced by the following:

Refunds for federally-registered LSVCCs

204.83 (1) Where a corporation is required, under subsections 204.82(3) and (4), to pay a tax and a penalty under this Part for a taxation year and, throughout any period of 12 consecutive months (in this section referred to as the "second period") that begins after the 12-month period in respect of which the tax became payable (in this section referred to as the "first period"), the corporation has no monthly deficiency and files with the Minister the return required under this Part for the taxation year in which the second period ends, the Minister shall refund to the corporation an amount equal to the total of the amount that was paid under subsection 204.82(3) and 80% of the amount that was paid under subsection 204.82(4) in respect of the first period.

Refunds for other LSVCCs

(2) Where

(*a*) the government of a province refunds, at any time, an amount to a corporation,

(*b*) the refund is of an amount that had been paid in satisfaction of a particular amount payable in a taxation year of the corporation, and

(*c*) tax was payable under subsection 204.82(5) by the corporation for a taxation year because the particular amount became payable,

the corporation is deemed to have paid at that time an amount equal to the refund on account of its tax payable under this Part for the year.

(2) Subsection (1) applies after February 18, 1997.

56. (1) Section 204.85 of the Act is replaced by the following:

Dissolution of federally-registered LSVCCs

204.85 (1) If a registered labour-sponsored venture capital corporation or a revoked corporation has issued any Class A shares, it shall not be amalgamated or merged with another corporation, or be liquidated or dissolved, except with the written permission of the Minister of Finance and on such terms and conditions as are specified by that Minister.

Dissolution of other LSVCCs

(2) Where

(*a*) an amount (other than interest on an amount to which this subsection applies or an amount payable under or as a consequence of a prescribed provision of a law of a province) is payable to the government of a province by a corporation,

(*b*) the amount is payable as a consequence of the amalgamation or merger of the corporation with another corporation, the winding-up or dissolution of the corporation or the corporation ceasing to be registered under a law of the province,

(*c*) the corporation has been prescribed for the purpose of the definition "approved share" in subsection 127.4(1), and

(*d*) the corporation is not a registered labour-sponsored venture capital corporation or a revoked corporation,

the corporation shall pay a tax under this Part for the taxation year in which the amount became payable equal to that amount.

(2) Subsection 204.85(1) of the Act, as enacted by subsection (1), applies after ANNOUNCEMENT DATE.

(3) Subsection 204.85(2) of the Act, as enacted by subsection (1), applies after February 18, 1997.

57. (1) Section 204.86 of the Act is replaced by the following:

Return and payment of tax for federally-registered LSVCCs

204.86 (1) Every registered labour-sponsored venture capital corporation and every revoked corporation shall

(*a*) on or before its filing-due date for a taxation year, file with the Minister a return for the year under this Part in prescribed form and containing prescribed information, without notice or demand therefor;

(*b*) estimate in the return the amount of tax and penalties, if any, payable under this Part by it for the year; and

(*c*) within 90 days after the end of the year, pay to the Receiver General the amount of tax and penalties, if any, payable under this Part by it for the year.

Return and payment of tax for other LSVCCs

(2) Where tax is payable under this Part for a taxation year by a corporation because of subsection 204.82(5) or 204.85(2), the corporation shall

(*a*) on or before its filing-due date for the year, file with the Minister a return for the year under this Part in prescribed form and containing prescribed information, without notice or demand therefor;

(*b*) estimate in the return the amount of tax payable under this Part by it for the year; and

(*c*) within 90 days after the end of the year, pay to the Receiver General the amount of tax payable under this Part by it for the year.

(2) Subsection (1) applies to taxation years that end after February 18, 1997.

58. (1) Subsection 204.9(1) of the Act is replaced by the following:

Definitions

204.9 (1) The definitions in this subsection apply in this Part.

"excess amount"
« excédent »

"excess amount" for a year at any time in respect of an individual means the amount, if any, by which the total of all contributions made after February 20, 1990, in the year and before that time into all registered education savings plans by or on behalf of all subscribers in respect of the individual exceeds the lesser of

(*a*) the RESP annual limit for the year, and

(*b*) the amount, if any, by which the RESP lifetime limit for the year exceeds the total of all contributions made into registered education savings plans by or on behalf of all subscribers in respect of the individual in all preceding years.

"RESP lifetime limit"
« plafond cumulatif de REEE »

"RESP lifetime limit" for a year means

(*a*) for the 1990 to 1995 years, $31,500; and

(*b*) for the 1996 and subsequent years, $42,000.

"subscriber's gross cumulative excess"
« excédent cumulatif brut du souscripteur »

"subscriber's gross cumulative excess" at any time in respect of an individual means the total of all amounts each of which is the subscriber's share of the excess amount for a relevant year at that time in respect of the individual, and for the purposes of this definition a relevant year at any time is a year that began before that time.

"subscriber's share of the excess amount"
« part du souscripteur sur l'excédent »

"subscriber's share of the excess amount" for a year at any time in respect of an individual means the amount determined by the formula

$$A/B \times C$$

where

A is the total of all contributions made after February 20, 1990, in the year and before that time into all registered education savings plans by or on behalf of the subscriber in respect of the individual;

B is the total of all contributions made after February 20, 1990, in the year and before that time into all registered education savings plans by or on behalf of all subscribers in respect of the individual; and

C is the excess amount for the year at that time in respect of the individual.

(2) Subsection 204.9(4) of the Act is replaced by the following:

New beneficiary

(4) For the purpose of this Part, where at any particular time an individual (in this subsection referred to as the "new beneficiary") becomes a beneficiary under a registered education savings plan in place of another individual (in this subsection referred to as the "former beneficiary") who ceased at or before the particular time to be a beneficiary under the plan,

(a) except as provided by paragraph (b), each contribution made at an earlier time by or on behalf of a subscriber into the plan in respect of the former beneficiary is deemed also to have been made at that earlier time in respect of the new beneficiary;

(b) except for the purpose of applying this subsection to a replacement of a beneficiary after the particular time, applying subsection (5) to a distribution after the particular time and applying subsection 204.91(3) to events after the particular time, paragraph (a) does not apply as a consequence of the replacement at the particular

time of the former beneficiary where the new beneficiary had not attained 21 years of age at the particular time and a parent of the new beneficiary was a parent of the former beneficiary; and

(c) except where paragraph (b) applies, each contribution made by or on behalf of a subscriber under the plan in respect of the former beneficiary under the plan is, without affecting the determination of the amount withdrawn from the plan in respect of the new beneficiary, deemed to have been withdrawn at the particular time from the plan to the extent that it was not withdrawn before the particular time.

Transfers between plans

(5) For the purpose of this Part, where property held by a trust governed by a registered education savings plan (in this subsection referred to as the "transferor plan") is distributed at a particular time to a trust governed by another registered education savings plan (in this subsection referred to as the "transferee plan"),

(*a*) except as provided by paragraphs (*b*) and (*c*), the amount of the distribution is deemed not to have been contributed into the transferee plan;

(*b*) subject to paragraph (*c*), each contribution made at any earlier time by or on behalf of a subscriber into the transferor plan in respect of a beneficiary under the transferor plan is deemed also to have been made at that earlier time by the subscriber in respect of each beneficiary under the transferee plan;

(*c*) except for the purpose of applying this subsection to a distribution after the particular time, applying subsection (4) to a replacement of a beneficiary after the particular time and applying subsection 204.91(3) to events after the particular time, paragraph (*b*) does not apply as a consequence of the distribution where

(i) any beneficiary under the transferee plan was, immediately before the particular time, a beneficiary under the transferor plan, or

(ii) a beneficiary under the transferee plan had not attained 21 years of age at the particular time and a parent of the beneficiary was a parent of an individual who was, immediately before the particular time, a beneficiary under the transferor plan;

(*d*) where subparagraph (*c*)(i) or (ii) applies in respect of the distribution, the amount of the distribution is deemed not to have been withdrawn from the transferor plan; and

(*e*) each subscriber under the transferor plan is deemed to be a subscriber under the transferee plan.

(3) Subsection (1) applies for the purpose of determining tax under Part X.4 of the Act for months that are after 1996.

(4) Subsection (2) applies to replacements of beneficiaries and distributions that occur after 1996.

59. (1) Section 204.91 of the Act is replaced by the following:

Tax payable by subscribers

204.91 (1) Every subscriber under a registered education savings plan shall pay a tax under this Part in respect of each month equal to 1% of the amount, if any, by which

(*a*) the total of all amounts each of which is the subscriber's gross cumulative excess at the end of the month in respect of an individual

exceeds

(*b*) the total of all amounts each of which is the portion of such an excess that has been withdrawn from a registered education savings plan before the end of the month.

Waiver of tax

(2) Where a subscriber under a registered education savings plan would, but for this subsection, be required to pay a tax in respect of a month under subsection (1) in respect of an individual, the Minister may waive or cancel all or part of the tax where it is just and equitable to do so having regard to all the circumstances, including

(*a*) whether the tax arose as a consequence of reasonable error;

(*b*) whether, as a consequence of one or more transactions or events to which subsections 204.9(4) or (5) apply, the tax is excessive; and

(*c*) the extent to which further contributions could be made into registered education savings plans in respect of the individual before the end of the month without causing additional tax to be payable

under this Part if this Part were read without reference to this subsection.

Marriage breakdown

(3) Where at any time an individual (in this subsection referred to as the "former subscriber") ceases to be a subscriber under a registered education savings plan as a consequence of the settlement of rights arising out of, or on the breakdown of, the marriage of the former subscriber and another individual (in this subsection referred to as the "current subscriber") who is a subscriber under the plan immediately after that time, for the purpose of determining tax payable under this Part in respect of a month that ends after that time, each contribution made before that time into the plan by or on behalf of the former subscriber is deemed to have been made into the plan by the current subscriber and not by or on behalf of the former subscriber.

Deceased subscribers

(4) For the purpose of applying this section where a subscriber has died, the subscriber's estate is deemed to be the same person as, and a continuation of, the subscriber for each month that ends after the death.

(2) Subsection 204.91(1) of the Act, as enacted by subsection (1), applies for the purpose of determining tax under Part X.4 of the Act for months that are after 1996.

(3) Subsection 204.91(2) of the Act, as enacted by subsection (1), applies for the purpose of determining tax under Part X.4 of the Act for months that are after January 1990.

(4) Subsections 204.91(3) and (4) of the Act, as enacted by subsection (1), apply for the purpose of determining tax under Part X.4 of the Act for months that are after 1997.

60. (1) The Act is amended by adding the following after Part X.4:

PART X.5

PAYMENTS UNDER

REGISTERED EDUCATION SAVINGS PLANS

Definitions

204.94 (1) The definitions in subsection 146.1(1) apply for the purposes of this Part, except that the definition "subscriber" in subsection 146.1(1) shall be read without reference to paragraph (*c*).

Charging provision

(2) Every person shall pay a tax under this Part for each taxation year equal to the amount determined by the formula

$$0.2 \times (A + B - C)$$

where

A is the total of all amounts each of which is an accumulated income payment made at any time

(*a*) either

(i) under a registered education savings plan under which the person is a subscriber at that time, or

(ii) under a registered education savings plan under which there is no subscriber at that time, where the person has been a spouse of an individual who was a subscriber under the plan, and

(*b*) that is included in computing the person's income under Part I for the year;

B is the total of all amounts each of which is an accumulated income payment that is

(*a*) not included in the value of A in respect of the person for the year, and

(*b*) included in computing the person's income under Part I for the year; and

C is the lesser of

(*a*) the lesser of the value of A in respect of the person for the year and the total of all amounts each of which is an amount deducted under subsection 146(5) or (5.1) in computing the person's income under Part I for the year, and

(*b*) the amount, if any, by which $40,000 exceeds the total of all amounts each of which is an amount determined under paragraph (*a*) in respect of the person for a preceding taxation year.

Return and payment of tax

(3) Every person who is liable to pay tax under this Part for a taxation year shall, on or before the person's filing-due date for the year,

(*a*) file with the Minister a return for the year under this Part in prescribed form and containing prescribed information, without notice or demand therefor;

(*b*) estimate in the return the amount of tax payable under this Part by the person for the year; and

(*c*) pay to the Receiver General the amount of tax payable by the person for the year.

Administrative rules

(4) Subsections 150(2) and (3), sections 152, 155 to 156.1, 158 to 167 and Division J of Part I apply with such modifications as the circumstances require.

(2) Subsection (1) applies to the 1998 and subsequent taxation years.

61. (1) The heading "TAX ON MINING RECLAMATION TRUSTS" before section 211.6 of the Act is replaced by the following:

TAX ON QUALIFYING ENVIRONMENTAL TRUSTS

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

62. (1) Subsections 211.6(1) to (4) of the Act are replaced by the following:

Charging provision

211.6 (1) Every trust that is a qualifying environmental trust at the end of a taxation year shall pay a tax under this Part for the year equal to 28% of its income under Part I for the year.

Computation of income

(2) For the purpose of subsection (1), the income under Part I of a qualifying environmental trust shall be computed as if this Act were read without reference to subsections 104(4) to (31) and sections 105 to 107.

Return

(3) Every trust that is a qualifying environmental trust at the end of a taxation year shall file with the Minister on or before its filing-due date for the year a return for the year under this Part in prescribed form containing an estimate of the amount of its tax payable under this Part for the year.

Payment of tax

(4) Every trust shall pay to the Receiver General its tax payable under this Part for each taxation year on or before its balance-due day for the year.

(2) Subsection (1) applies to the 1997 and subsequent taxation years.

63. (1) Paragraph 212(1)(*r*) of the Act is replaced by the following:

Registered education savings plan

(*r*) a payment that is

(i) required by paragraph 56(1)(*q*) to be included in computing the non-resident person's income under Part I for a taxation year, and

(ii) not required to be included in computing the non-resident person's taxable income or taxable income earned in Canada for the year;

(2) Subsection (1) applies to amounts paid or credited after February 28, 1979.

64. (1) Paragraph 214(3)(*j*) of the Act is repealed.

(2) Subsection (1) applies after 1997.

65. Section 241 of the Act is amended by adding the following after subsection (3.1):

Registered charities

(3.2) An official may provide to any person the following taxpayer information relating to a charity that at any time was a registered charity:

(*a*) a copy of the charity's governing documents, including its statement of purpose;

(*b*) any information provided in prescribed form to the Minister by the charity upon applying for registration under this Act;

(*c*) the names of the persons who at any time were the charity's directors and the periods during which they were its directors;

(*d*) a copy of the notification of the charity's registration, including any conditions and warnings; and

(*e*) where the registration of the charity has been revoked, a copy of any letter sent by or on behalf of the Minister to the charity relating to the grounds for the revocation.

66. (1) The definition "mining reclamation trust" in subsection 248(1) of the Act is repealed.

(2) Paragraph (*e*.2) of the definition "cost amount" in subsection 248(1) of the Act is replaced by the following:

(*e*.2) where the property is an interest of a beneficiary under a qualifying environmental trust, nil, and

(3) Subsection 248(1) of the Act is amended by adding the following in alphabetical order:

"private foundation"
« *fondation privée* »

"private foundation" has the meaning assigned by subsection 149.1(1);

"public foundation"
« *fondation publique* »

"public foundation" has the meaning assigned by subsection 149.1(1);

"qualifying environmental trust"
« *fiducie pour l'environnement admissible* »

"qualifying environmental trust" at any time means a trust resident in a province and maintained at that time for the sole purpose of funding the reclamation of a site in the province that had been used primarily for, or for any combination of, the operation of a mine, the extraction of clay, peat, sand, shale or aggregates (including dimension stone and gravel) or the deposit of waste, where the maintenance of the trust is or may become required under the terms of a contract entered into with Her Majesty in right of Canada or the province or is or may become required pursuant to a law of Canada or the province and the contract was entered into or that law was enacted, as the case may be, on or before the later of January 1, 1996 and the day that is one year after the day on which the trust was created, but does not include a trust

(*a*) that relates at that time to the reclamation of a well,

(*b*) that is not maintained at that time to secure the reclamation obligations of one or more persons or partnerships that are beneficiaries under the trust,

(*c*) that at that time has a trustee other than

(i) Her Majesty in right of Canada or the province, or

(ii) a corporation resident in Canada that is licensed or otherwise authorized under the laws of Canada or a province to carry on in Canada the business of offering to the public its services as trustee,

(*d*) that borrows money at that time,

(*e*) that acquired at that time any property that is not described in any of paragraphs (*a*), (*b*) and (*f*) of the definition "qualified investment" in section 204,

(*f*) to which the first contribution was made before 1992,

(*g*) from which any amount was distributed before February 23, 1994,

(*h*) where that time is before 1998 and the trust is not a mining reclamation trust at that time,

(i) to which the first contribution was made before 1996,

(ii) from which any amount was distributed before February 19, 1997, or

(iii) any interest in which was disposed of before February 19, 1997,

(*i*) that elected in writing filed with the Minister, before 1998 or before April of the year following the year in which the first contribution to the trust was made, never to have been a qualifying environmental trust, or

(*j*) that was at any previous time during its existence not a qualifying environmental trust;

"total pension adjustment reversal"
« facteur global de rectification »

"total pension adjustment reversal" of a taxpayer for a calendar year has the meaning assigned by regulation;

(4) Subsection (1) applies after 1997 and, where an election is made by a trust in accordance with paragraph (*i*) of the definition "qualifying environmental trust" in subsection 248(1) of the Act, as enacted by subsection (3),

(*a*) the trust is deemed to have never been a mining reclamation trust, and

(*b*) notwithstanding subsections 152(4) to (5) of the Act, the Minister of National Revenue may before 2000 make such assessments and reassessments as are necessary to give effect to the election.

(5) Subsection (2) applies after 1995.

(6) The definitions "private foundation" and "public foundation" in subsection 248(1) of the Act, as enacted by subsection (3), apply after 1996.

(7) The definition "qualifying environmental trust" in subsection 248(1) of the Act, as enacted by subsection (3), applies after 1991.

(8) The definition "total pension adjustment reversal" in subsection 248(1) of the Act, as enacted by subsection (3) applies after 1996.

67. (1) Subsection 250(7) of the Act is replaced by the following:

Residence of a qualifying environmental trust

(7) For the purposes of this Act, where a trust resident in Canada would be a qualifying environmental trust at any time if it were resident at that time in the province in which the site to which the trust relates is situated, the trust is deemed to be resident at that time in that province and in no other province.

(2) Subsection (1) applies after 1995.

PART II

ANNUITY CONTRACTS AS QUALIFIED INVESTMENT FOR RRSPs AND RRIFs

DIVISION A

INCOME TAX ACT

68. (1) Clauses 60(*l*)(ii)(A) and (B) of the *Income Tax Act* are replaced by the following:

(A) under which the taxpayer is the annuitant

(I) for the taxpayer's life, or for the lives jointly of the taxpayer and the taxpayer's spouse either without a guaranteed period, or with a guaranteed period that is not greater than 90 years minus the lesser of the age in whole years of the taxpayer and the age in whole years of the taxpayer's spouse at the time the annuity was acquired, or

(II) for a term equal to 90 years minus the age in whole years of the taxpayer or the age in whole years of the taxpayer's spouse, at the time the annuity was acquired, or

(B) under which the taxpayer, or a trust under which the taxpayer is the sole person beneficially interested in amounts payable under the annuity, is the annuitant for a term not exceeding 18 years minus the age in whole years of the taxpayer at the time the annuity was acquired

(2) Subsection (1) applies to the 1989 and subsequent taxation years.

69. (1) Paragraph (*c*) of the definition "qualified investment" in subsection 146(1) of the Act is replaced by the following:

(*c*) an annuity described in the definition "retirement income" in respect of the annuitant under the plan, if purchased from a licensed annuities provider,

(*c*.1) a contract for an annuity issued by a licensed annuities provider where

(i) the trust is the only person who, disregarding any subsequent transfer of the contract by the trust, is or may

become entitled to any annuity payments under the contract, and

(ii) the holder of the contract has a right to surrender the contract at any time for an amount that would, if reasonable sales and administration charges were ignored, approximate the value of funds that could otherwise be applied to fund future periodic payments under the contract,

(*c*.2) a contract for an annuity issued by a licensed annuities provider where

(i) annual or more frequent periodic payments are or may be made under the contract to the holder of the contract,

(ii) the trust is the only person who, disregarding any subsequent transfer of the contract by the trust, is or may become entitled to any annuity payments under the contract,

(iii) neither the time nor the amount of any payment under the contract may vary because of the length of any life, other than the life of the annuitant under the plan (in this definition referred to as the "RRSP annuitant"),

(iv) the day on which the periodic payments began or are to begin (in this paragraph referred to as the "start date") is no later than the end of the year in which the RRSP annuitant attains 70 years of age,

(v) either

(A) the periodic payments are payable for the life of the RRSP annuitant and either there is no guaranteed period under the contract or there is a guaranteed period beginning at the start date that does not exceed a term equal to 90 years minus the lesser of

(I) the age in whole years at the start date of the RRSP annuitant (determined on the assumption that the RRS P annuitant is alive at the start date), and

(II) the age in whole years at the start date of a spouse of the RRSP annuitant (determined on the assumption that a spouse of the RRSP annuitant at the time the contract was acquired is a spouse of the RRSP annuitant at the start date), or

(B) the periodic payments are payable for a term equal to

(I) 90 years minus the age described in subclause (A)(I), or

(II) 90 years minus the age described in subclause (A)(II), and

(vi) the periodic payments are equal, or are not equal solely because of one or more adjustments that would, if the contract were an annuity under a retirement savings plan, be in accordance with subparagraphs (3)(*b*)(iii) to (v) or that arise because of a uniform reduction in the entitlement to the periodic payments as a consequence of a partial surrender of rights to the periodic payments, and

(2) Section 146 of the Act is amended by adding the following after subsection (11):

Exception

(11.1) Subsection (11) does not apply to annuity contracts issued after 1997.

(3) Subsection (1) applies after 1996.

(4) Subsection (2) applies after 1997.

70. (1) The definition "minimum amount" in subsection 146.3(1) of the Act is replaced by the following:

"minimum amount"
« *minimum* »

"minimum amount" under a retirement income fund for a year is the amount determined by the formula

$$(A \times B) + C$$

where

A is the total fair market value of all properties held in connection with the fund at the beginning of the year (other than annuity contracts held by a trust governed by the fund that, at the beginning of the year, are not described in paragraph (*b*.1) of the definition "qualified investment");

B is

(*a*) where the first annuitant under the fund elected in respect of the fund under paragraph (*b*) of the definition "minimum amount" in this subsection, as it read before 1992, or under subparagraph 146.3(1)(*f*)(i) of the *Income Tax Act*, chapter 148 of the Revised Statutes of Canada, 1952, to use the age of another individual, the prescribed factor for the year in respect of the other individual,

(*b*) where paragraph (*a*) does not apply and the first annuitant under the fund so elects before any payment has been made under the fund by the carrier, the prescribed factor for the year in respect of an individual who was the spouse of the first annuitant at the time of the election, and

(*c*) in any other case, the prescribed factor for the year in respect of the first annuitant under the fund; and

C is, where the fund governs a trust, the total of all amounts each of which is

(*a*) a periodic payment under an annuity contract held by the trust at the beginning of the year (other than an annuity contract described at the beginning of the year in paragraph (*b*.1) of the definition "qualified investment") that is paid to the trust in the year, or

(*b*) where the periodic payment under such an annuity contract is not made to the trust because the trust disposed of the right to that payment in the year, a reasonable estimate of that payment on the assumption that the annuity contract had been held throughout the year and no rights under the contract were disposed of in the year;

(2) The definition "qualified investment" in subsection 146.3(1) of the Act is amended by striking out the word "and" at the end of paragraph (*b*) and by adding the following after paragraph (*b*):

(*b*.1) a contract for an annuity issued by a licensed annuities provider where

(i) the trust is the only person who, disregarding any subsequent transfer of the contract by the trust, is or may become entitled to any annuity payments under the contract, and

(ii) the holder of the contract has a right to surrender the contract at any time for an amount that would, if reasonable sales and administration charges were ignored, approximate the value of funds that could otherwise be applied to fund future periodic payments under the contract,

(*b*.2) a contract for an annuity issued by a licensed annuities provider where

(i) annual or more frequent periodic payments are or may be made under the contract to the holder of the contract,

(ii) the trust is the only person who, disregarding any subsequent transfer of the contract by the trust, is or may become entitled to any annuity payments under the contract,

(iii) neither the time nor the amount of any payment under the contract may vary because of the length of any life, other than

(A) where the annuitant under the fund (in this paragraph referred to as the "RRIF annuitant") has made the election referred to in the definition "retirement income fund" in respect of the fund and a spouse, the life of the RRIF annuitant or the life of the spouse, and

(B) in any other case, the life of the RRIF annuitant,

(iv) the day on which the periodic payments began or are to begin (in this paragraph referred to as the "start date") is no later than the end of the year following the year in which the contract was acquired by the trust,

(v) either

(A) the periodic payments are payable for the life of the RRIF annuitant or the joint lives of the RRIF annuitant and the RRIF annuitant's spouse and either there is no guaranteed period under the contract or there is a guaranteed period beginning at the start date that does not exceed a term equal to 90 years minus the lesser of

(I) the age in whole years at the start date of the RRIF annuitant (determined on the assumption that the RRIF annuitant is alive at the start date), and

(II) the age in whole years at the start date of a spouse of the RRIF annuitant (determined on the assumption that a spouse of the RRIF annuitant at the time the

contract was acquired is a spouse of the RRIF annuitant at the start date), or

(B) the periodic payments are payable for a term equal to

(I) 90 years minus the age described in subclause (A)(I), or

(II) 90 years minus the age described in subclause (A)(II), and

(vi) the periodic payments are equal, or are not equal solely because of one or more adjustments that would, if the contract were an annuity under a retirement savings plan, be in accordance with subparagraphs 146(3)(*b*)(iii) to (v) or that arise because of a uniform reduction in the entitlement to the periodic payments as a consequence of a partial surrender of rights to the periodic payments, and

(3) Paragraph 146.3(2)(*e*) of the Act is replaced by the following:

(*e*) the fund provides that, at the direction of the annuitant, the carrier shall, in prescribed form and manner, transfer all or part of the property held in connection with the fund, or an amount equal to its value at the time of the direction (other than property required to be retained in accordance with the provision described in paragraph (*e*.1) or (*e*.2)), together with all information necessary for the continuance of the fund, to a person who has agreed to be a carrier of another registered retirement income fund of the annuitant;

(4) The portion of paragraph 146.3(2)(*e*.1) of the Act preceding subparagraph (i) is replaced by the following:

(*e*.1) where the fund does not govern a trust or the fund governs a trust created before 1998 that does not hold an annuity contract as a qualified investment for the trust, the fund provides that where an annuitant, at any time, directs that the carrier transfer all or part of the property held in connection with the fund, or an amount equal to its value at that time, to a person who has agreed to be a carrier of another registered retirement income fund of the annuitant, the transferor shall retain an amount equal to the lesser of

(5) Subsection 146.3(2) of the Act is amended by adding the following after paragraph (*e*.1):

(*e*.2) where paragraph (*e*.1) does not apply, the fund provides that where an annuitant, at any time, directs that the carrier transfer all or part of the property held in connection with the fund, or an amount

equal to its value at that time, to a person who has agreed to be a carrier of another registered retirement income fund of the annuitant, the transferor shall retain property in the fund sufficient to ensure that the total of

(i) all amounts each of which is the fair market value, immediately after the transfer, of a property held in connection with the fund that is

(A) property other than an annuity contract, or

(B) an annuity contract described, immediately after the transfer, in paragraph (*b*.1) of the definition "qualified investment" in subsection (1), and

(ii) all amounts each of which is a reasonable estimate, as of the time of the transfer, of the amount of an annual or more frequent periodic payment under an annuity contract (other than an annuity contract described in clause (i)(B)) that the trust may receive after the transfer and in the year of the transfer

is not less than the amount, if any, by which the minimum amount under the fund for that year exceeds the total of all amounts received out of or under the fund before the transfer that are included in computing the income of the annuitant under the fund for that year;

(6) Subsection (1) applies

(*a*) to the 1998 and subsequent years with respect to

(i) retirement income funds entered into after February 1986, and

(ii) retirement income funds entered into before March 1986 and revised or amended after February 1986 and before 1998;

(*b*) to the year in which a retirement income fund is first revised or amended after 1997 and to subsequent years, where the fund was entered into before March 1986 and was not revised or amended after February 1986 and before 1998; and

(*c*) with respect to a retirement income fund that governs a trust that, after Announcement Date, holds a contract for an annuity, to all years that begin after the first day

(i) that is after Announcement Date, and

(ii) on which the trust holds such a contract.

(7) Subsection (2) applies after 1996.

(8) Subsections (3) to (5) apply to retirement income funds entered into after July 13, 1990.

71. (1) Subsection 248(1) of the Act is amended by adding the following in alphabetical order:

"licensed annuities provider"
« *fournisseur de rentes autorisé* »

"licensed annuities provider" has the meaning assigned by subsection 147(1);

(2) Subsection (1) applies after 1996.

DIVISION B

INCOME TAX CONVENTIONS INTERPRETATION ACT

72. (1) Paragraph (*c*) of the definition "periodic pension payment" in section 5 of the *Income Tax Conventions Interpretation Act* is replaced by the following:

(*c*) a payment at any time in a calendar year under a registered retirement income fund, where the total of all payments (other than the specified portion of each such payment) made under the fund at or before that time and in the year exceeds the total of

(i) the amount that would be the greater of

(A) twice the amount that, if the value of C in the definition "minimum amount" in subsection 146.3(1) of the *Income Tax Act* were nil, would be the minimum amount under the fund for the year, and

(B) 10% of the fair market value of the property (other than annuity contracts that, at the beginning of the year, are not described in paragraph (*b*.1) of the definition "qualified investment" in subsection 146.3(1) of the *Income Tax Act*) held in connection with the fund at the beginning of the year

if all property transferred in the year and before that time to the carrier of the fund as consideration for the carrier's undertaking to make payments under the fund had been so

transferred immediately before the beginning of the year and if the definition "minimum amount" in subsection 146.3(1) of the *Income Tax Act* applied with respect to all registered retirement income funds, and

(ii) the total of all amounts each of which is an annual or more frequent periodic payment under an annuity contract that is a qualified investment, as defined in subsection 146.3(1) of the *Income Tax Act*, (other than an annuity contract the fair market value of which is taken into account under clause (i)(B)) held by a trust governed by the fund that was paid into the trust in the year and before that time; or

(2) Subsection (1) applies to amounts paid after 1997.

73. (1) Section 5.1 of the Act is renumbered as subsection 5.1(1) and is amended by adding the following:

Definition of "specified portion"

(2) For the purpose of the definition "periodic pension payment" in section 5, the "specified portion" of a payment means

(*a*) the portion of the payment that is not required by section 146.3 of the *Income Tax Act* to be included in computing the income of any person and that is not included under paragraph 212(1)(*q*) of that Act in respect of any person; and

(*b*) the portion of the payment in respect of which a deduction is available under paragraph 60(*l*) of the *Income Tax Act* in computing the income of any person.

(2) Subsection (1) applies to amounts paid after 1997.

PART III

ROLLOVERS TO REGISTERED PENSION PLAN ANNUITIES

74. (1) The portion of paragraph 147.1(3)(*a*) of the *Income Tax Act* before subparagraph (i) is replaced by the following:

(*a*) subject to paragraph (*b*), the plan is, for the purposes of this Act other than paragraphs 60(*j*) and (*j*.2) and sections 147.3 and 147.4, deemed to be a registered pension plan throughout the period that begins on the latest of

(2) Subsection (1) applies after 1996.

75. (1) Paragraph 147.3(10)(*a*) of the Act is replaced by the following:

(*a*) the amount is deemed to have been paid from the transferor plan to the individual; and

(2) Subsection 147.3(15) of the Act is repealed.

(3) Subsection (1) applies to transfers that occur on or after ANNOUNCEMENT DATE.

(4) Subsection (2) applies after 1996.

76. (1) The Act is amended by adding the following after section 147.3:

RPP annuity contract

147.4 (1) Where

(*a*) at any time an individual acquires, in full or partial satisfaction of the individual's entitlement to benefits under a registered pension plan, an interest in an annuity contract purchased from a licensed annuities provider,

(*b*) the rights provided for under the contract are not materially different from those provided for under the plan as registered,

(*c*) the contract does not permit premiums to be paid at or after that time, other than a premium paid at that time out of or under the plan to purchase the contract,

(*d*) either the plan is not a plan in respect of which the Minister may, under subsection 147.1(11), give a notice of intent to revoke the registration of the plan or the Minister waives the application of this paragraph with respect to the contract and so notifies the administrator of the plan in writing, and

(*e*) the individual does not acquire the interest as a consequence of a transfer of property from the plan to a registered retirement savings plan or a registered retirement income fund,

the following rules apply for the purposes of this Act:

(*f*) the individual is deemed not to have received an amount out of or under the registered pension plan as a consequence of acquiring the interest, and

(*g*) other than for the purposes of sections 147.1 and 147.3, any amount received at or after that time by any individual under the contract is deemed to have been received under the registered pension plan.

Amended contract

(2) Where

(*a*) an amendment is made at any time to an annuity contract to which subsection (1) or paragraph 254(*a*) applies (other than an amendment the sole effect of which is to provide for an earlier annuity commencement that avoids the application of paragraph (4)(*b*)), and

(*b*) the rights provided for under the contract are materially altered as a consequence of the amendment,

the following rules apply for the purposes of this Act:

(*c*) each individual who has an interest in the contract immediately before that time is deemed to have received at that time the payment of an amount under a pension plan equal to the fair market value of the interest immediately before that time,

(*d*) the contract as amended is deemed to be a separate annuity contract issued at that time otherwise than pursuant to or under a superannuation or pension fund or plan, and

(*e*) each individual who has an interest in the separate annuity contract immediately after that time is deemed to have acquired the

interest at that time at a cost equal to the fair market value of the interest immediately after that time.

New contract

(3) For the purposes of this Act, where an annuity contract (in this subsection referred to as the "original contract") to which subsection (1) or paragraph 254(*a*) applies is, at any time, substituted by another contract,

(*a*) if the rights provided for under the other contract are not materially different from those provided for under the original contract, the other contract is deemed to be the same contract as, and a continuation of, the original contract; and

(*b*) in any other case, each individual who has an interest in the original contract immediately before that time is deemed to have received at that time the payment of an amount under a pension plan equal to the fair market value of the interest immediately before that time.

RPP annuity contract commencing after age 69

(4) For the purposes of this Act, where, under circumstances to which paragraph 254(*a*) applied, an individual acquired before 1997 an interest in an annuity contract in full or partial satisfaction of the individual's entitlement to benefits under a registered pension plan, and payment of the annuity has not begun by the end of the particular year in which the individual attains 69 years of age,

(*a*) the interest is deemed not to exist after the particular year;

(*b*) the individual is deemed to have received immediately after the particular year the payment of an amount from the plan equal to the fair market value of the interest at the end of the particular year;

(*c*) the individual is deemed to have acquired immediately after the particular year an interest in the contract as a separate annuity contract issued immediately after the particular year at a cost equal to the amount referred to in paragraph (*b*); and

(*d*) the issue and acquisition of the separate annuity contract are deemed not to be pursuant to or under a registered pension plan.

(2) Subsections 147.4(1) to (3) of the Act, as enacted by subsection (1), apply to annuity contract acquisitions, amendments and substitutions that occur on or after ANNOUNCEMENT DATE.

(3) Subsection 147.4(4) of the Act, as enacted by subsection (1), applies after 1996, except that

(*a*) it does not apply to an individual who attained 70 years of age before 1997;

(*b*) in applying subsection 147.4(4), as enacted by subsection (1), to an individual who attained 69 years of age in 1996, the reference in that provision to "69 years of age" shall be read as a reference to "70 years of age"; and

(*c*) subsection 147.4(4), as enacted by subsection (1), does not apply to an annuity contract where an individual received an interest in the contract before March 6, 1996 and, under the terms and conditions of the contract as they read immediately before that day,

(i) the day on which the annuity payments are to begin under the contract is fixed and determined and is after the year in which the individual attains

(A) 69 years of age, where the individual had not attained that age before 1997, or

(B) 70 years of age, where the individual attained 69 years of age in 1996, and

(ii) the amount and timing of each annuity payment are fixed and determined.

77. (1) The portion of section 254 of the Act before paragraph (*b*) is replaced by the following:

Contract under pension plan

254. Where a document has been issued or a contract has been entered into before ANNOUNCEMENT DATE purporting to create, to establish, to extinguish or to be in substitution for, a taxpayer's right to an amount or amounts, immediately or in the future, out of or under a superannuation or pension fund or plan,

(*a*) if the rights provided for in the document or contract are rights provided for by the superannuation or pension plan or are rights to

a payment or payments out of the superannuation or pension fund, and the taxpayer acquired an interest under the document or in the contract before that day, any payment under the document or contract is deemed to be a payment out of or under the superannuation or pension fund or plan and the taxpayer is deemed not to have received, by the issuance of the document or entering into the contract, an amount out of or under the superannuation or pension fund or plan; and

(2) Subsection (1) applies on and after ANNOUNCEMENT DATE.

PART IV

MATCHABLE EXPENDITURES

78. (1) Subsection 12(1) of the *Income Tax Act* is amended by adding, immediately after paragraph (g), the following:

Proceeds of disposition of right to receive production

(*g*.1) any proceeds of disposition to which subsection 18.1(6) applies;

(2) Subsection (1) applies to dispositions that occur after November 17, 1996.

79. (1) The Act is amended by adding the following after section 18:

Definitions

18.1 (1) The definitions in this subsection apply to this section.

"matchable expenditure" ***« dépense à rattacher »***

"matchable expenditure" of a taxpayer means the amount of an expenditure that is made by the taxpayer to

(*a*) acquire a right to receive production,

(*b*) fulfil a covenant or obligation arising in circumstances where it is reasonable to conclude that there is a relationship existing between the covenant or obligation and a right to receive production, or

(*c*) preserve or protect a right to receive production,

but does not include an amount for which a deduction is provided under section 20 in computing the taxpayer's income.

"right to receive production"
« droit aux produit »

"right to receive production" means a right under which a taxpayer is entitled, either immediately or in the future and either absolutely or contingently, to receive an amount all or any portion of which is computed by reference to use of property, production, revenue, profit, cash flow, commodity price, cost or value of property or any other similar criterion or by reference to dividends paid or payable to shareholders of any class of shares where the amount is in respect of another taxpayer's activity, property or business but such a right does not include an income interest in a trust, a Canadian resource property or a foreign resource property.

"tax benefit"
« avantage fiscal »

"tax benefit" means a reduction, avoidance or deferral of tax or other amount payable under this Act or an increase in a refund of tax or other amount under this Act.

"tax shelter"
« abri fiscal »

"tax shelter" means a property that would be a tax shelter (as defined in subsection 237.1(1)) if

(*a*) the cost of a right to receive production were the total of all amounts each of which is a matchable expenditure to which the right relates; and

(*b*) subsections (2) to (13) did not apply for the purpose of computing an amount, or in the case of a partnership a loss, represented to be deductible.

"taxpayer"
« contribuable »

"taxpayer" includes a partnership.

Limitation on the deductibility of matchable expenditure

(2) In computing a taxpayer's income from a business or property for a taxation year, no amount of a matchable expenditure may be deducted except as provided by subsection (3).

Deduction of matchable expenditure

(3) Where a taxpayer's matchable expenditure would but for subsection (2) and this subsection be deductible in computing the taxpayer's income, there may be deducted in respect of the matchable expenditure in computing the taxpayer's income for a taxation year the amount that is determined under subsection (4) for the year in respect of the expenditure.

Amount of deduction

(4) For the purpose of subsection (3), the amount determined under this subsection for a taxation year in respect of a taxpayer's matchable expenditure is the amount, if any, that is the least of

(*a*) the total of

(i) the lesser of

(A) 1/5 of the matchable expenditure, and

(B) the amount determined by the formula

$$A/B \times C$$

where

A is the number of months that are in the year and after the day on which the right to receive production to which the matchable expenditure relates is acquired,

B is lesser of 240 and the number of months that are in the period that begins on the day on which the right to receive production to which the matchable expenditure relates is acquired and ends on the day that right is to terminate, and

C is the amount of the matchable expenditure, and

(ii) the amount, if any, by which the amount determined under this paragraph for the preceding taxation year in respect of the matchable expenditure exceeds the amount of the matchable expenditure deductible in computing the taxpayer's income for that preceding year;

(*b*) the total of

(i) all amounts each of which is included in computing the taxpayer's income for the year (other than any portion of such amount that is the subject of a reserve claimed by the taxpayer for the year under this Act) in respect of the right to receive production to which the matchable expenditure relates, and

(ii) the amount by which the amount determined under this paragraph for the preceding taxation year in respect of the matchable expenditure exceeds the amount of the matchable expenditure deductible in computing the taxpayer's income for that preceding year; and

(*c*) the amount, if any, by which

(i) the total of all amounts each of which is an amount of the matchable expenditure that would, but for this section, have been deductible in computing the taxpayer's income for the year or a preceding taxation year

exceeds

(ii) the total of all amounts each of which is an amount of the matchable expenditure deductible under subsection (3) in computing the taxpayer's income for a preceding taxation year.

Special rules

(5) For the purpose of this section,

(*a*) where a taxpayer's matchable expenditure is made before the day on which the related right to receive production is acquired by the taxpayer, the expenditure is deemed to have been made on that day;

(*b*) where a taxpayer has one or more rights to renew a particular right to receive production to which a matchable expenditure relates for one or more additional terms, after the term that includes the time at which the particular right was acquired, the particular right is deemed to terminate on the latest day on which the latest possible

such term could terminate if all rights to renew the particular right were exercised;

(*c*) where a taxpayer has 2 or more rights to receive production that can reasonably be considered to be related to each other, the rights are deemed to be one right; and

(*d*) where the term of a taxpayer's right to receive production is for an indeterminate period, the right is deemed to terminate 240 months after it is acquired.

Proceeds of disposition considered income

(6) Where in a taxation year a taxpayer disposes of all or part of a right to receive production to which a matchable expenditure relates, the proceeds of the disposition shall be included in computing the taxpayer's income for the year.

Arm's length disposition

(7) Subject to subsections (8) to (10), where in a taxation year a taxpayer disposes (otherwise than in a disposition to which subsection 87(1) or 88(1) applies) of all of the taxpayer's right to receive production to which a matchable expenditure (other than an expenditure no portion of which would, if this section were read without reference to this subsection, be deductible under subsection (3) in computing the taxpayer's income) relates, or the taxpayer's right expires, the amount deductible in respect of the expenditure under subsection (3) in computing the taxpayer's income for the year is deemed to be the amount, if any, determined under paragraph (4)(c) for the year in respect of the expenditure.

Non-arm's length disposition

(8) Subsection (10) applies where

(*a*) a taxpayer's particular right to receive production to which a matchable expenditure (other than an expenditure no portion of which would, if this section were read without reference to subsections (7) and (10), be deductible under subsection (3) in computing the taxpayer's income) relates has expired or the taxpayer has disposed of all of the right (otherwise than in a disposition to which subsection 87(1) or 88(1) applies);

(*b*) during the period that begins 30 days before and ends 30 days after the disposition or expiry, the taxpayer or a person affiliated, or who does not deal at arm's length, with the taxpayer acquires a right to receive production (in this subsection and subsection (10) referred to as the "substituted property") that is, or is identical to, the particular right; and

(*c*) at the end of the period, the taxpayer or a person affiliated, or who does not deal at arm's length, with the taxpayer owns the substituted property.

Special case

(9) Subsection (10) applies where

(*a*) a taxpayer's particular right to receive production to which a matchable expenditure (other than an expenditure no portion of which would, if this section were read without reference to subsections (7) and (10), be deductible under subsection (3) in computing the taxpayer's income) relates has expired or the taxpayer has disposed of all of the right (otherwise than in a disposition to which subsection 87(1) or 88(1) applies); and

(*b*) during the period that begins at the time of the disposition or expiry and ends 30 days after that time, a taxpayer that had an interest, directly or indirectly, in the right has another interest, directly or indirectly, in another right to receive production, which other interest is a tax shelter or a tax shelter investment (as defined by section 143.2).

Amount of deduction if non-arm's length disposition

(10) Where this subsection applies because of subsection (8) or (9) to a disposition or expiry in a taxation year or a preceding taxation year of a taxpayer's right to receive production to which a matchable expenditure relates,

(*a*) the amount deductible under subsection (3) in respect of the expenditure in computing the taxpayer's income for a taxation year that ends at or after the disposition or expiry of the right is the least of the amounts determined under subsection (4) for the year in respect of the expenditure; and

(*b*) the least of the amounts determined under subsection (4) in respect of the expenditure for a taxation year is deemed to be the

amount, if any, determined under paragraph (4)(*c*) in respect of the expenditure for the year where the year includes the time that is immediately before the first time, after the disposition or expiry,

(i) at which the right would, if it were owned by the taxpayer, be deemed by section 128.1 or subsection 149(10) to have been disposed of by the taxpayer,

(ii) that is immediately before control of the taxpayer is acquired by a person or group of persons, where the taxpayer is a corporation,

(iii) at which winding-up of the taxpayer begins (other than a winding-up to which subsection 88(1) applies), where the taxpayer is a corporation,

(iv) where subsection (8) applies, at which a 30-day period begins throughout which neither the taxpayer nor a person affiliated, or who does not deal at arm's length, with the taxpayer owns

(A) the substituted property, or

(B) a property that is identical to the substituted property and that was acquired after the day that is 31 days before the period began, or

(v) where subsection (9) applies, at which a 30-day period begins throughout which no taxpayer who had an interest, directly or indirectly, in the right has an interest, directly or indirectly, in another right to receive production if one or more of those direct or indirect interests in the other right is a tax shelter or tax shelter investment (as defined by section 143.2).

Partnerships

(11) For the purpose of paragraph (10)(*b*), where a partnership otherwise ceases to exist at any time after a disposition or expiry referred to in subsection (10), the partnership is deemed not to have ceased to exist, and each taxpayer who was a member of the partnership immediately before the partnership would, but for this subsection, have ceased to exist is deemed to remain a member of the partnership until the time that is immediately after the first of the times described in subparagraphs (10)(*b*)(i) to (v).

Identical property

(12) For the purposes of subsections (8) and (10), a right to acquire a particular right to receive production (other than a right, as security

only, derived from a mortgage, agreement of sale or similar obligation) is deemed to be a right to receive production that is identical to the particular right.

Application of section 143.2

(13) For the purpose of applying section 143.2 to an amount that would, if this section were read without reference to this subsection, be a matchable expenditure any portion of the cost of which is deductible under subsection (3), the expenditure is deemed to be a tax shelter investment and that section shall be read without reference to subparagraph 143.2(6)(*b*)(ii).

Debt Obligations

(14) Where the rate of return on a taxpayer's right to receive production to which a matchable expenditure (other than an expenditure no portion of which would, if this section were read without reference to this subsection, be deductible under subsection (3) in computing the taxpayer's income) relates, is reasonably certain at the time the taxpayer acquires the right,

(*a*) the right is, for the purposes of subsection 12(9) and Part LXX of the *Income Tax Regulations*, deemed to be a debt obligation in respect of which no interest is stipulated to be payable in respect of its principal amount and the obligation is deemed to be satisfied at the time the right terminates for an amount equal to the total of the return on the obligation and the amount that would otherwise be the matchable expenditure that is related to the right; and

(*b*) notwithstanding subsection (3), no amount may be deducted in computing the taxpayer's income in respect of any matchable expenditure that relates to the right.

Non-applicability of section 18.1

(15) Subject to subsections (1) and (14), this section does not apply to a taxpayer's matchable expenditure in respect of a right to receive production where no portion of the expenditure can reasonably be considered to have been paid to another taxpayer, or a person with whom the other taxpayer does not deal at arm's length, to acquire the right from the other taxpayer and

(*a*) the taxpayer's expenditure cannot reasonably be considered to relate to a tax shelter or tax shelter investment (as defined by section 143.2) and none of the main purposes for making the

expenditure is that the taxpayer, or a person with whom the taxpayer does not deal at arm's length, obtain a tax benefit; or

(*b*) before the end of the taxation year in which the expenditure is made, the total of all amounts each of which is included in computing the taxpayer's income for the year (other than any portion of such amount that is the subject of any reserve claimed by the taxpayer for the year under this Act) in respect of the right to receive production to which the matchable expenditure relates exceeds 80% of the expenditure.

(2) Subsection (1) applies to an expenditure made by a taxpayer or a partnership after November 17, 1996 other than, in respect of a particular right to receive production, such an expenditure made

(*a*) before 1997 pursuant to an agreement in writing made by the taxpayer or the partnership before 1997 to acquire the particular right

(i) in return for paying selling commissions incurred before 1997 in connection with the distribution of shares of a mutual fund corporation or units of mutual fund trust, or

(ii) to render production services before 1997 for a film or video production,

and, for the purpose of applying this paragraph, the expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made and, where subparagraph (ii) applies, only to the extent the services are rendered at or before that time,

(*b*) before August 1997 where

(i) the expenditure is made pursuant to an agreement in writing made by the taxpayer or the partnership before August 1997 to acquire the particular right in return for paying selling commissions incurred after 1996 and before August 1997 in connection with the distribution of shares of a mutual fund corporation or units of a mutual fund trust that is managed by an administrator of mutual funds,

(ii) the particular right to receive production is identified in an advance income tax ruling request delivered to Revenue Canada before November 18, 1996,

(iii) the total of all such expenditures made by any taxpayer or partnership in respect of all of the rights identified in the

advance income tax ruling request does not exceed $30,000,000, and

(iv) all tax shelter investments (as defined by section 143.2 of the Act) that can reasonably be considered to relate to the expenditure are acquired before August 1997,

and, for the purpose of applying this paragraph, an expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made,

(*c*) before August 1997 where

(i) the expenditure is made pursuant to an agreement in writing made by the taxpayer or the partnership before August 1997 to acquire the particular right in return for paying selling commissions incurred after 1996 and before August 1997 in connection with the distribution of shares of a mutual fund corporation or units of a mutual fund trust that is managed by an administrator of mutual funds, other than by an administrator of a mutual fund that is or is related to an administrator to which paragraph (*b*) refers in respect of commissions incurred in connection with the distribution of the shares or units described in paragraph (*b*),

(ii) the total of all such expenditures made by any taxpayer or partnership to acquire particular rights in return for paying selling commissions in connection with the distribution of shares of the mutual fund corporation or units of the mutual fund trust that is managed by the administrator of mutual funds or any other person that is related to the administrator does not exceed $10,000,000, and

(iii) all tax shelter investments (as defined by section 143.2 of the Act) that can reasonably be considered to relate to the expenditure are acquired before August 1997,

and, for the purpose of applying this paragraph, an expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made,

(*d*) before August 1997 pursuant to an agreement in writing made by the taxpayer or the partnership before August 1997 to acquire the particular right and to render production services before August 1997 for a film or video production where

(i) at least 75% of the expenditures made in respect of the film or video production by the taxpayer or partnership pertain to services performed in Canada by residents of Canada, and

(ii) all tax shelter investments (as defined by section 143.2 of the Act) that can reasonably be considered to relate to the expenditure are acquired before August 1997,

and, for the purpose of applying this paragraph, the expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made and only to the extent the services are rendered at or before that time,

(*e*) before 1998, pursuant to an agreement in writing made by the taxpayer or the partnership before November 18, 1996 to acquire the particular right, and for this purpose where the expenditure relates to service obligations to be fulfilled by the taxpayer or partnership, the expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made and only to the extent the services are rendered at or before that time,

(*f*) before 1998, pursuant to the terms of a document that is a prospectus, preliminary prospectus or registration statement where

(i) the document was filed before November 18, 1996 with a public authority in Canada in accordance with the securities legislation of Canada or of any province and, where required by law, accepted for filing by the public authority,

(ii) the particular right is identified in the document, and

(iii) all the funds raised pursuant to the document were raised before 1997 and all tax shelter investments (as defined by section 143.2 of the Act), that can reasonably be considered to relate to the expenditure, are acquired before August 1997,

and, for the purpose of applying this paragraph, where an expenditure relates to service obligations to be fulfilled by the taxpayer or partnership, the expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made and only to the extent the services are rendered at or before that time, or

(*g*) before 1998, pursuant to the terms of an offering memorandum distributed as part of an offering of securities where

(i) the memorandum contained a complete or substantially complete description of the securities contemplated in the offering as well as the terms and conditions of the offering,

(ii) the memorandum was distributed before November 18, 1996,

(iii) solicitations in respect of the sale of the securities contemplated by the memorandum were made before November 18, 1996,

(iv) the sale of the securities was substantially in accordance with the memorandum,

(v) the particular right is identified in the document, and

(vi) all the funds raised pursuant to the memorandum were raised before 1997 and all tax shelter investments (as defined by section 143.2 of the Act), that can reasonably be considered to relate to the expenditure, are acquired before August 1997,

and, for the purpose of applying this paragraph, where an expenditure relates to service obligations to be fulfilled by the taxpayer or partnership, the expenditure is deemed to have been made no earlier than the time and only to the extent it is considered for the purposes of the Act to have been made and only to the extent the services are rendered at or before that time,

except that paragraphs (*e*), (*f*) and (*g*) apply to an expenditure only if

(*h*) there is no agreement or other arrangement under which the obligations of the taxpayer or the partnership with respect to the expenditure can be changed, reduced or waived if there is a change to the Act or if there is an adverse assessment under the Act,

(*i*) where the expenditure is associated with one or more tax shelters sold or offered for sale at a time and in circumstances in which section 237.1 of the Act requires an identification number to have been obtained, the identification number was obtained before that time, and

(*j*) in the case of an expenditure, including an expenditure to which paragraph (*e*) applies, made pursuant to a document described in paragraph (*f*) or (*g*), a portion of the securities authorized to be sold in 1996 pursuant to the document were after 1995 and before November 18, 1996 sold to, or subscribed for by, a person who was not at the time of sale or subscription

(i) a promoter, or an agent of a promoter, of the securities,

(ii) a grantor of the right to receive production to which the expenditure relates,

(iii) a broker or dealer in securities, or

(iv) a person who did not deal at arm's length with a person referred to in subparagraph (i) or (ii).

80. (1) Paragraph 87(2)(*j*.2) of the Act is replaced by the following:

Prepaid expenses and matchable expenditures

(*j*.2) for the purposes of subsections 18(9) and (9.01), section 18.1 and paragraph 20(1)(*mm*), the new corporation is deemed to be the same corporation as, and a continuation of, each predecessor corporation;

(2) Subsection (1) applies after November 17, 1996.

81. (1) Subparagraph 88(1)(*a*)(i) of the Act is replaced by the following:

(i) in the case of a Canadian resource property, a foreign resource property or a right to receive production (as defined in subsection 18.1(1)) to which a matchable expenditure (as defined in subsection 18.1(1)) relates, nil, and

(2) Subsection (1) applies after November 17, 1996.

82. (1) Paragraph (*e*) of the definition "cost amount" in subsection 248(1) of the Act is amended by striking out the word "or" at the end of subparagraph (ii), by adding the word "or" at the end of subparagraph (iii) and by adding the following after subparagraph (iii):

(iv) a right to receive production (as defined in subsection 18.1(1)) to which a matchable expenditure (as defined in subsection 18.1(1)) relates,

(2) Subsection (1) applies after November 17, 1996.

83. (1) The portion of subsection 256(7) of the Act before paragraph (*a*) is replaced by the following:

Acquiring control

(7) For the purposes of subsections 10(10), 13(21.1) and (24), 14(12) and 18(15), sections 18.1 and 37, subsection 40(3.4), the definition "superficial loss" in section 54, section 55, subsections 66(11), (11.4) and (11.5), 66.5(3) and 66.7(10) and (11), section 80, paragraph 80.04(4)(*h*), subsections 85(1.2) and 88(1.1) and (1.2), sections 111 and 127, subsection 249(4) and this subsection

(2) Subsection (1) applies after April 26, 1995, except that before November 18, 1996 the reference in subsection 256(7) of the Act, as enacted by subsection (1), to "sections 18.1 and 37" shall be read as "section 37".

SCHEDULE II

BILL C-69

Change to Application Rule

for subsections 112(3) to (3.32)

of the *Income Tax Act*, as proposed in Bill C-69

(10) Subsections 112(3) to (3.32) of the Act, as enacted by subsection (1), apply to dispositions that occur after April 26, 1995, other than

(*a*) a disposition that occurs pursuant to an agreement in writing made before April 27, 1995;

(*b*) a disposition of a share of the capital stock of a corporation that is made to the corporation where

(i) on April 26, 1995 the share was owned by an individual (other than a trust) or a particular trust under which an individual (other than a trust) was a beneficiary,

(ii) on April 26, 1995 a corporation, or a partnership of which a corporation is a member, was a beneficiary of a life insurance policy that insured the life of the individual or the individual's spouse,

(iii) it was reasonable to conclude on April 26, 1995 that a main purpose of the life insurance policy was to fund, directly or indirectly, in whole or in part, a redemption, acquisition or cancellation of the share by the corporation that issued the share, and

(iv) the disposition is made by

(A) the individual or the individual's spouse,

(B) the estate of the individual or of the individual's spouse within the estate's first taxation year,

(C) the particular trust where it is a trust described in paragraph 104(4)(*a*) or (*a*.1) of the Act in respect of a spouse, the spouse is the beneficiary referred to in subparagraph (i) and the disposition occurs before the end of the trust's third taxation year that begins after the spouse's death, or

(D) a trust described in paragraph 73(1)(*c*) of the Act created by the individual in respect of the individual's spouse, or a trust described in paragraph 70(6)(*b*) of the Act created by the individual's will in respect of the individual's spouse, before the end of the trust's third taxation year that begins after the spouse's death;

(c) a disposition of a share of the capital stock of a corporation owned by an individual on April 26, 1995 that is made by the individual's estate before 1997;

(d) a disposition of a share of the capital stock of a corporation owned by an estate on April 26, 1995, the first taxation year of which ended after that date, that is made by the estate before 1997; or

(e) a disposition of a share of the capital stock of a corporation owned by an individual on April 26, 1995 where the individual is a trust described in paragraph 104(4)(*a*) or (*a*.1) of the Act in respect of a spouse, that is made by the trust after the spouse's death and before 1997.

(11) For the purposes of paragraph (10)(*b*) and this subsection, a share of the capital stock of a corporation acquired in exchange for another share in a transaction to which section 51, 85, 86 or 87 of the Act applies is deemed to be the same share as the other share.

Explanatory Notes

PREFACE

These explanatory notes relate to proposed amendments to the *Income Tax Act* and the *Income Tax Conventions Interpretation Act*. These notes describe these proposed amendments, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

The Honourable Paul Martin
Minister of Finance

These explanatory notes are provided to assist in an understanding of proposed amendments to the *Income Tax Act* and the *Income Tax Conventions Interpretation Act*. These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

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SCHEDULE I

PART I

EXPLANATORY NOTES TO DRAFT AMENDMENTS

1997 BUDGET INCOME TAX PROPOSALS

Clause 1

Income from Business or Property

ITA
12

Section 12 of the *Income Tax Act* provides for the inclusion of various amounts in computing the income of a taxpayer for a taxation year from a business or property.

ITA
12(1)(*z*.1) and (*z*.2)

Paragraph 12(1)(*z*.1) of the Act provides that any amount received by a taxpayer in the taxpayer's capacity as a beneficiary of a mining reclamation trust is to be included in computing the taxpayer's income for tax purposes. Paragraph 12(1)(*z*.2) provides that consideration received by a taxpayer for the sale of the taxpayer's interest as a beneficiary of a mining reclamation trust is also generally included in computing the taxpayer's income.

Paragraphs 12(1)(*z*.1) and (*z*.2) are amended so that each reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". These amendments are in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

These amendments apply to taxation years that end after February 18, 1997.

Clause 2

Prohibited Deductions

ITA
18

Section 18 of the Act prohibits the deduction of certain outlays and expenses in computing a taxpayer's income from a business or property.

ITA
18(11)

Paragraphs 20(1)(*c*), (*d*), (*e*), (*e*.1) and (*f*) of the Act permit deductions for interest and certain other financing expenses relating to borrowed money used by a taxpayer for the purpose of earning money from a business or property. These provisions are, however, subject to subsection 18(11) which prohibits the deduction of such expenses in respect of indebtedness incurred for the purposes of making a contribution to an RRSP or certain other deferred income plans.

Subsection 18(11) is amended to ensure that interest and similar expenses are not deductible in respect of borrowed money used to contribute to a registered education savings plan.

This amendment applies to 1998 and subsequent taxation years.

Clause 3

Income from a Business or Property - Deductions

ITA
20

Section 20 of the Act provides rules relating to the deductibility of certain outlays, expenses and other amounts in computing a taxpayer's income for a taxation year from a business or property.

ITA
20(1)(*ss*) and (*tt*)

Paragraph 20(1)(*ss*) of the Act provides that contributions made by a taxpayer to a mining reclamation trust of which the taxpayer is a beneficiary are deductible in computing the taxpayer's income for the taxation year in which the contributions were made.

Paragraph 20(1)(*tt*) of the Act generally provides that any consideration paid by a taxpayer for the acquisition of an interest in a mining reclamation trust is deductible in computing the taxpayer's income for the year of acquisition.

These provisions are amended so that the references to "mining reclamation trust" are replaced by broader references to "qualifying environmental trust". These amendments are in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

These amendments apply to taxation years that end after February 18, 1997. However, a special transitional rule applies in the case of qualifying environmental trusts (other than mining reclamation trusts) to which contributions were first made after 1995 but before February 19, 1997. In this case, contributions made before February 19, 1997 will be considered to be made on February 19, 1997 so that they will qualify for deduction under paragraph 20(1)(*ss*).

Clause 4

Scientific Research and Experimental Development

ITA
37

Section 37 of the Act sets out rules for the deductibility of expenditures incurred by a taxpayer for scientific research and experimental development (SR&ED).

ITA
37(12)

Subsection 37(11) generally provides that, in order to deduct an amount as a scientific research and experimental development (SR&ED) expenditure under subsection 37(1), the taxpayer must file a form with Revenue Canada within one year of the taxpayer's filing-due date for the year in which the expenditure was incurred, identifying the expenditure and supporting its characterization as SR&ED.

Subsection 37(12) of the existing Act provides that the filing requirement in subsection 37(11) does not apply where an expenditure is reclassified by the Minister of National Revenue as an expenditure on or in respect of scientific research and experimental development.

Amended subsection 37(12) deems an expenditure in respect of which the taxpayer has not met the filing requirement in subsection 37(11) not to be an expenditure on or in respect of scientific research and experimental development. This will cause the expenditure to be classified in accordance with the scheme of the Act, but without reference to the provisions relating to scientific research and experimental development. For example, an expenditure on equipment, which would have been an SR&ED capital expenditure if the prescribed form had been filed on time, would generally be treated as depreciable property, while an expenditure which would have been an SR&ED current expenditure would generally be deductible as a current expense under section 9.

This amendment applies to the 1997 and subsequent taxation years.

Clause 5

Taxable Capital Gains

ITA
38(*a*) and (*a*.1)

The portion of a taxpayer's capital gain that is required to be included in computing income is his or her "taxable capital gain".

New paragraph 38 (*a*.1) provides that if a capital gain results from the making of a gift to a qualified donee of a security listed on a stock exchange, a share or unit of a mutual fund, an interest in a segregated fund or a prescribed debt obligation, only 3/8 of the gain will be a taxable capital gain and hence included in income. For this purpose a qualified donee means any person, other than a private charitable foundation, to whom gifts may be made that qualify for the charitable donations deduction or tax credit. It is intended that "prescribed debt obligation" be defined by regulation to include certain debt obligations that have a readily determinable market value such as government bonds. This amendment applies to gifts made after February 18, 1997 and before 2002.

Clause 6

Meaning of Capital Gain and Capital Loss

ITA
39

Section 39 of the Act sets out the meaning of capital gain, capital loss and business investment loss and provides a number of special rules relating to capital gains.

Subclause 6(1)

ITA
39(1)(*a*)(v)

A taxpayer's capital gain for a taxation year from the disposition of property is determined under paragraph 39(1)(*a*) of the Act. Because of subparagraph 39(1)(*a*)(v), a disposition of an interest of a beneficiary under a mining reclamation trust does not give rise to any capital gain.

Subparagraph 39(1)(*a*)(v) is amended so that the reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". This amendment is in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

This amendment applies to taxation years that end after February 18, 1997.

Subclause 6(2)

Labour-sponsored Venture Capital Corporations

ITA
39(5)

Subsection 39(5) of the Act provides a list of taxpayers who are not entitled to the election under subsection 39(4) to treat any gain or loss arising on disposition of Canadian securities as a capital gain or loss.

Subsection 39(5) is amended to exclude from the list a taxpayer that is a mutual fund corporation or a mutual fund trust. This amendment clarifies that prescribed labour-sponsored venture capital corporations (which under subsection 131(8) are generally treated as mutual fund corporations) and other mutual funds can elect to treat each gain or loss arising on a disposition of a Canadian security as a capital gain or capital loss.

This amendment generally applies to the 1991 and subsequent taxation years. In addition, under a transitional rule, a mutual fund corporation or mutual fund trust has until its filing-due date for its first taxation year that includes the date of Royal Assent to file the election required under subsection 39(4) in prescribed form. In these circumstances, the election applies from the taxation year specified in the election provided that the specified year is no earlier than its 1991 taxation year and no later than its taxation year that includes the date of Royal Assent.

It should be noted that it is intended that a parallel change will be made to paragraph (*c*) of the definition "eligible corporation" in subsection 5100(1) of the *Income Tax Regulations* to exclude mutual fund corporations from the application of that paragraph for the 1991 and subsequent taxation years.

Clause 7

Capital Gains

ITA
40(1.01)

When a taxpayer makes a charitable gift of a non-qualifying security new subsections 110.1(6) and 118.1(13) of the Act provide that the gift will be ignored for the purposes of the charitable donations deduction and tax credit, respectively. However, if the donee disposes of the security within five years the donor will be treated as having made a gift at that later time. New subsection 40(1.01) of the Act is introduced in order to permit the taxpayer to claim a reserve in respect of any gain realized from the making of the original gift so that the resulting inclusion in income can be shifted to a later year, including, in particular, the year in which the donor ultimately receives recognition under section 110.1 or 118.1 for the donation. The new reserve to be claimed under paragraph 40(1.01)(*c*) is available only in taxation years ending within 60 months of the making of the gift. Moreover, the reserve cannot be claimed once the taxpayer receives tax recognition for the gift nor if the taxpayer becomes non-resident or tax-exempt. This amendment applies to the 1997 and subsequent taxation years.

Clause 8

Amounts Included in Income

ITA
56

Section 56 of the Act lists income of certain types that are required to be included in computing the income of a taxpayer from sources other than property, business and employment.

Subclause 8(1)

ITA
56(1)(*a*)(i) and (*a*.1)

Subparagraph 56(1)(*a*)(i) of the Act includes in the income of a taxpayer for a taxation year certain pension benefits received in the year, including death benefits under the Canada Pension Plan (CPP) and Quebec Pension Plan (QPP).

Subparagraph 56(1)(*a*)(i) is amended so that any CPP/QPP death benefit is ignored under that subparagraph. Instead, any CPP/QPP death benefit received after Announcement Date in respect of the death of an individual will be included under new paragraph 56(1)(*a*.1) in the income of the estate that arose on or as a consequence of the death of the individual.

These amendments apply to 1997 and subsequent taxation years. However, any CPP/QPP death benefit in respect of the death of an individual received by the individual's estate on or before Announcement Date is not covered by these amendments.

Subclause 8(2)

CPP/QPP Benefits for Previous Years

ITA
56(8)

Subsection 56(8) of the Act allows an individual to exclude from income in the year of receipt CPP/QPP disability benefits that relate to one or more prior years (except where the prior year benefits are less than $300) and to pay tax on those benefits as if they had been received in the prior years to which they relate. This amendment broadens the application of subsection 56(8) to all CPP/QPP benefits of at least $300 that relate to prior years.

This amendment applies to benefits received after 1995.

Clause 9

Child Care Expenses

ITA
63(3)

Section 63 of the Act provides rules concerning the deductibility of child care expenses in computing an individual's income. Subsection 63(3) contains the definition "earned income". In any year, an individual is not allowed to deduct child care expenses in excess of two-thirds of earned income for that year.

This amendment to the English version of the definition "earned income" is consequential on the amendment to paragraph 56(8)(*a*). It ensures that, while all types of benefits received under the Canada and Quebec Pension Plans may be eligible for the special tax treatment provided under that paragraph, only disability pensions paid under those plans may be included in computing an individual's earned income for the purposes of the child care expense deduction.

This amendment applies to amounts received after 1995.

Clause 10

Attendant Care Expenses

ITA
64

Section 64 of the Act permits the deduction, in computing the income of an individual who has a severe and prolonged mental or physical impairment, of expenses paid to an attendant (other than the individual's spouse) who is at least 18 years of age that are incurred

to enable the individual to work. Such an individual is entitled under the existing Act to deduct the least of the three following amounts:

- the actual amount of expenses for attendant care provided in Canada,
- 2/3 of the individual's earned income for the year, and
- $5,000.

These amendments, which apply to 1997 and subsequent taxation years, eliminate the $5,000 limitation.

Clause 11

Reserves for Year of Death

ITA
72(1)(*c*)

Paragraph 72(1)(*c*) of the Act denies the deductibility of the capital gains reserves in subparagraphs 40(1)(*a*)(iii) and 44(1)(*e*)(iii) in the year in which a taxpayer dies. This amendment adds a reference to new paragraph 40(1.01)(*c*) of the Act so that a taxpayer will not be able to claim this special reserve, which is available in respect of a gain arising from the making of a charitable donation of a non-qualifying security, in the year of death. This amendment applies to the 1997 and subsequent taxation years.

Clause 12

Attribution Rule

ITA
75

Section 75 of the Act provides that where a person transfers property to a trust under certain conditions, any income from the property is attributed to the transferor.

ITA
75(3)(*c*.1)

Subsection 75(3) of the Act exempts income from property held by mining reclamation trusts and certain other trusts from the attribution rule in subsection 75(2).

Paragraph 75(3)(*c*.1) is amended so that the reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". This amendment is in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

This amendment applies to taxation years that end after February 22, 1994.

Clause 13

Amounts not Included in Income

ITA
81(1)(*o*) and (*p*)

Paragraph 81(1)(*o*) of the Act provides that a "refund of payments" (as defined in subsection 146.1(1)) under an education savings plan is not to be included in computing a taxpayer's income. Paragraph 81(1)(*p*) provides that an "educational assistance payment" received by a beneficiary from a non-registered or revoked education savings plan is likewise not included in computing a taxpayer's income.

Paragraph 81(1)(*o*) is repealed by this amendment because it is unnecessary. There is nothing in the Act that would otherwise include a "refund of payments" in computing a taxpayer's income.

Paragraph 81(1)(*p*) is also repealed. Because subsection 146.1(14) is being repealed, no amount is included in the income of a subscriber upon the revocation of a registered education savings plan. Consequently, it is no longer appropriate to exclude educational assistance payments from revoked registered retirement saving plans

from income. In addition, it is not appropriate to provide an income exclusion for an education savings plan that has never been registered.

These amendments apply to 1998 and subsequent taxation years.

Clause 14

Amalgamations

ITA
87(2)(*m*.1)

New subsection 40(1.01) of the Act permits a taxpayer to claim a reserve in respect of a capital gain arising from the making of a charitable donation of a non-qualifying security. Where two or more companies amalgamate new paragraph 87(2)(*m*.1) of the Act treats the amalgamated company as a continuation of each of its predecessors so that if a predecessor claimed a reserve under paragraph 40(1.01)(*c*) in its last taxation year the same amount will be included under paragraph 40(1.01)(*b*) in the amalgamated company's income for its first taxation year. By virtue of paragraph 88(1)(*e*.2) of the Act this rule applies equally upon the winding-up of a wholly-owned subsidiary into its parent corporation. This amendment applies to the 1997 and subsequent taxation years.

Clause 15

Windings-Up

ITA
88(1)(*e*.61)

In certain circumstances new subsections 110.1(6) and 118.1(13) of the Act will apply to treat a wholly-owned subsidiary corporation that has been wound up as having made a charitable donation after the corporation has ceased to exist. In such cases new paragraph 88(1)(*e*.61) will apply to treat the gift as having been made by the subsidiary's parent corporation so that it may claim the

resulting deduction under section 110.1 in computing its taxable income. This amendment applies after Announcement Date.

Clause 16

Public Corporation

ITA
89(1)
"public corporation"

Subsection 89(1) of the Act contains the definition "public corporation" which, by virtue of subsection 248(1), is relevant for all purposes of the Act.

The definition is amended to provide that a prescribed labour-sponsored venture capital corporation is not a public corporation for the purposes of the Act unless a class of its shares becomes listed on a prescribed stock exchange in Canada. For this purpose, it is intended that section 6701 of the Regulations will be amended to add a cross reference to this definition.

This amendment applies to the 1995 and subsequent taxation years.

Clause 17

Beneficiaries of Qualifying Environmental Trusts

ITA
107.3

Section 107.3 of the Act sets out a number of rules dealing with the taxation of the beneficiaries of "mining reclamation trusts", as defined in subsection 248(1).

Section 107.3 is amended so that each reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". Similarly, a reference to a "mine" is replaced by a broader reference to a "site". These amendments are in consequence of the extension of the rules for mining reclamation

trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

Subsection 107.3(3) is also amended so that, in the event that a trust ceases to be a qualifying environmental trust at any time, the taxation year of the trust is deemed to have ended immediately before that time (rather than at that time, as is provided under the existing provision). Consequently, tax under Part XII.4 will apply to the trust for the taxation year that is deemed to have ended because of the change in status.

These amendments apply to taxation years that end after February 18, 1997.

Clause 18

Trusts - Definitions

ITA
108

Section 108 of the Act sets out certain definitions and rules that apply for the purposes of subdivision k of Division B of Part I of the Act which deals with the taxation of trusts and their beneficiaries.

ITA
108(1)

"preferred beneficiary"

Subsection 108(1) of the Act defines the expression "preferred beneficiary", which is relevant for the purpose of the preferred beneficiary election in subsection 104(14). A preferred beneficiary for a trust's taxation year is essentially an individual who

- is resident in Canada,

- is a beneficiary under the trust at the end of the trust's taxation year who is entitled to a disability tax credit under

subsection 118.3(1) of the Act for the individual's taxation year in which the trust's taxation year ends, and

- is the trust settlor, the settlor's spouse or former spouse, a child, grandchild or great-grandchild of the settlor or a spouse of such a person.

The definition "preferred beneficiary" is amended so that the requirement that the beneficiary under a trust be entitled to a tax credit under subsection 118.3(1) is satisfied for a trust taxation year where the beneficiary is entitled to the tax credit for the beneficiary's taxation year that ends in the trust year. This amendment affects only testamentary trusts with non-calendar year ends. It ensures that trustees of a testamentary trust will know, with greater certainty, the status of a beneficiary by the time a preferred beneficiary election is made in respect of the beneficiary.

This definition is also amended to provide that an adult is not excluded as a "preferred beneficiary" for a trust taxation year because the adult is not entitled to the tax credit under subsection 118.3(1), where the adult is a dependant (within the meaning assigned by subsection 118(6)) of another individual for the adult's taxation year that ends in the trust year because of mental or physical infirmity and an income test is satisfied. The income test is satisfied where the adult's income (computed without reference to any amount designated under a preferred beneficiary election and allocated to the adult) for the adult's year that ends in the trust year does not exceed $6,456. The $6,456 limit is the same as the income limit used for the purposes of the dependant tax credit under subsection 118(1) of the Act. Amended subsection 117.1(1) of the Act provides for the indexing of this new limit.

These amendments apply to trust taxation years that end after 1996.

Clause 19

Charitable Donations Deduction

ITA
110.1

Section 110.1 of the Act provides for the deductibility in computing taxable income of charitable donations and certain other gifts made by corporations.

Subclause 19(1)

ITA
110.1(1) and (1.1)

Subsection 110.1(1) of the Act provides for the deduction of a corporation's charitable donations, gifts to the Crown and certain gifts of cultural property and ecologically sensitive land. Donors may carry forward unused deductions for up to five years.

Under the existing Act the deduction for charitable donations is limited to 50% of the corporation's net income for the year of the donations, plus 50% of any taxable capital gains resulting from the making of the donations. Crown gifts and gifts of cultural property and ecologically sensitive land are not subject to this limitation under the existing Act. The present amendment provides that both charitable gifts and Crown gifts are to be subject to a new deduction limit, namely, 75% of the corporation's net income, 25% of any taxable capital gain resulting from the gifts plus 25% of any recapture of depreciation included in income as a result of the making of the gifts. This new limitation applies to gifts made in taxation years that begin after 1996, except that there will be no limitation on Crown gifts made before February 19, 1997 nor on Crown gifts made pursuant to an agreement in writing made before that date.

New subsection 110.1(1.1) of the Act contains two rules governing the deductibility of charitable donations and other gifts under subsection 110.1(1). The first rule is that once the amount of a gift has been deducted in a taxation year it may not be carried forward to be deducted again in a future year. This rule is now contained in the definition of each of the four types of gift in subsection 110.1(1).

The second rule, in paragraph 110.1(1.1)(*b*), is that gifts will be considered to be deducted in the order that they were made. This "first-in, first-out" assumption reflects Revenue Canada's interpretation of section 110.1 of the existing Act and is the assumption most favourable to taxpayers. New subsection 110.1(1.1) applies in computing taxable income for taxation years that begin after 1996.

Subclause 19(2)

ITA
110.1(5) to (7)

Certain gifts of ecologically sensitive land are deductible under paragraph 110.1(1)(*d*) of the Act in computing a corporate donor's taxable income. For this purpose "land" includes a covenant, easement or servitude to which land is subject. As it is generally difficult to establish the fair market value of these rights, new subsection 110.1(5) of the Act is introduced to provide that the fair market value of a gift of a covenant, easement or servitude will not be considered to be less than the decrease in value of the subject land that resulted from the making of the gift. This amendment applies to gifts made after February 27, 1995.

New subsections 118.1(13) and (15) to (18) of the Act apply to deny or defer an individual's charitable donations tax credit in certain circumstances. New subsection 110.1(6) provides that those rules are to apply equally in determining a corporation's charitable donations deduction. Where because of new subsection 118.1(13) a corporation's deduction for a charitable donation would be deferred until after the corporation has ceased to exist, new subsection 110.1(7) of the Act treats the corporation as having made the donation in its last taxation year. An exception is provided for corporations which have ceased to exist as a result of an amalgamation under subsection 87(1) or a winding-up under subsection 88(1). In that case the new corporation or the parent corporation will be treated under paragraph 87(2)(*v*) or 88(1)(*e*.61), respectively, as having made the donation at the time provided for in new subsection 118.1(13). These amendments apply after Announcement Date.

Clause 20

Annual Adjustment of Deductions and Other Amounts

ITA
117.1(1)

Subsection 117.1(1) of the Act provides for the indexing of various amounts, including the amounts on which the personal tax credits are based. The indexing is based on annual increases in the Consumer Price Index in excess of 3%.

These amendments renumber existing paragraphs 117.1(1)(*a*) and (*a*.1) of the Act as paragraphs 117.1(1)(*b*.1) and (*b*.2), respectively. This change, effective for 1997 and subsequent taxation years, allows for the insertion of new paragraph 117.1(1)(*a*).

New paragraph 117.1(1)(*a*) and further amendments to subsection 117.1(1) provide for the indexing after 1996 of the $6,456 income limit for preferred beneficiaries, described in the commentary to the amended definition "preferred beneficiary" in subsection 108(1) of the Act. These amendments apply to 1997 and subsequent taxation years.

Paragraph 117.1(1)(*b*.2) is amended as a consequence of new section 122.51 of the Act dealing with the refundable medical expense supplement for low-income earners. The $500 maximum amount of the supplement, as well as the threshold amounts of $2,500 and $16,069, will also be indexed. This amendment applies to 1998 and subsequent taxation years.

Clause 21

Charitable Donations Tax Credit

ITA
118.1

Section 118.1 of the Act provides the tax credit that may be claimed by individuals who make charitable donations, gifts to the Crown and

certain gifts of cultural property and ecologically sensitive land. Donors may carry forward unused claims for up to five years.

Subclauses 21(1) to (4)

ITA
118.1(1)

Subsection 118.1(1) of the Act provides definitions of various terms for purposes of the charitable donations tax credit, including "total gifts" which is the amount on which the tax credit is determined under subsection 118.1(3) of the Act.

Under the existing Act the amount of charitable donations that may be included in an individual's total gifts for a taxation year is limited to 50% of the individual's net income for the year plus 50% of any taxable capital gains resulting from the making of the donations. Crown gifts and gifts of cultural property and ecologically sensitive land are not subject to this limitation under the existing Act. The amendments to subsection 118.1(1) provide that both an individual's charitable donations and gifts to the Crown are to be subject to a new limit on inclusion in the individual's total gifts, namely, 75% of the individual's net income, 25% of any taxable capital gains resulting from the gifts (to the extent that they were not excluded from the individual's taxable income by the lifetime capital gains exemption in section 110.6 of the Act) plus 25% of any recapture of depreciation included in income as a result of the making of the gifts. This new limitation applies to gifts made in taxation years that begin after 1996, except that there will be no limitation on Crown gifts made before February 19, 1997 nor on Crown gifts made pursuant to agreements in writing made before that date.

Subclause 21(5)

ITA
118.1(2.1)

New subsection 118.1(2.1) of the Act provides that gifts will be considered to have been claimed in determining an individual's charitable donations tax credits in the order in which they were made. This "first-in, first-out" assumption reflects Revenue Canada's interpretation of section 118.1 of the existing Act and is the

assumption most favourable to taxpayers. New subsection 118.1(2.1) applies to taxation years that begin after 1996.

Subclause 21(6)

ITA
118.1(4) and (5)

Subsection 118.1(4) of the Act treats a gift made in the year of an individual's death as having been made in the preceding year to the extent that it was not deducted in the year of death. This provision is modified in two ways. First, this amendment clarifies that subsection 118.1(4) is subject to subsection 118.1(13) of the Act so that where an individual has made a gift of a non-qualifying security in the year in which the individual died the gift will not be considered to have been made in the preceding year because of the application of subsection 118.1(4), but rather paragraph 118.1(13)(*a*) applies to treat the gift as not having been made. Secondly, the amendment ensures that where a gift is deemed to have been made by an individual in the year of death under subsection 118.1(5) (gift made by will) or subsection 118.1(14) (gift deemed to have been made when donee disposes of a non-qualifying security), subsection 118.1(4) will apply to treat the gift as having been made in the year preceding the year of the death. This amendment applies to gifts made after Announcement Date.

Subsection 118.1(5) of the Act treats a gift made by an individual's will as having been made in the year of death. This amendment clarifies that, where a gift of a non-qualifying security is made by a will, subsection 118.1(13) of the Act is to prevail to treat the gift as not having been made. This amendment applies to gifts made after Announcement Date.

Subclause 21(7)

ITA
118.1(12) to (18)

Certain gifts of ecologically sensitive land are included in an individual's "total ecological gifts" (as defined in subsection 118.1(1) of the Act) for the purpose of determining the individual's charitable donations tax credit. For this purpose "land" includes a covenant,

easement or servitude to which land is subject. As it is generally difficult to establish the fair market value of these rights, new subsection 118.1(12) of the Act is introduced to provide that the fair market value of a gift of a covenant, easement or servitude will not be considered to be less than the decrease in value of the subject land that resulted from the making of the gift. This amendment applies to gifts made after February 27, 1995.

New subsection 118.1(13) of the Act provides that if an individual makes a gift of a non-qualifying security, that gift will be ignored for the purpose of the charitable donations tax credit. However, if the donee disposes of the security within five years the individual will be treated as having made a gift at that later time. The fair market value of the later gift will be considered to be the lesser of two amounts: the first amount is the consideration received by the donee for the disposition (except to the extent that the consideration is another non-qualifying security of the individual); the second amount is the fair market value of the original gift.

For the purpose of new subsections 118.1(13) and (15), new subsection 118.1(17) of the Act defines a non-qualifying security of an individual to be an obligation of the individual or a non-arm's length person, a share issued by a corporation with which the individual does not deal at arm's length or any other security issued by the individual or a non-arm's length person. Specifically excepted from this definition are obligations, shares and other securities listed on prescribed stock exchanges and deposits with financial institutions. For this purpose "financial institution" is defined in new subsection 118.1(18) of the Act as being a member of the Canadian Payments Association or a credit union that is a shareholder or member of a central for the purposes of the Canadian Payments Association Act.

Where an individual makes a gift of a non-qualifying security and dies before the donee disposes of the gift within the prescribed five-year period, new subsection 118.1(14) of the Act will apply to treat the subsequently resulting gift as having been made by the individual in the year of death, rather than at the time of the disposition by the donee.

New subsection 118.1(15) of the Act applies in two cases. The first case occurs where an individual makes a gift, the donee holds a

non-qualifying security of the individual within five years thereafter and the donee acquired the security no earlier than five years before the gift was made. The second case occurs where an individual makes a gift to a non-arm's length donee, the individual or a non-arm's length person uses property of the donee within five years thereafter, the use of the property was pursuant to an agreement made no earlier than five years before the making of the gift and the use of the property was not in the course of the donee's charitable activities. In either of these cases the fair market value of the gift will be reduced for the purpose of the individual's charitable donations tax credit. In the case of the acquisition of a non-qualifying security the gift's value will be reduced by the fair market value of the consideration given by the donee to acquire the security. In the case of the use of property, the gift will be reduced by the fair market value of the property. New subsections 118.1(13) to (15) generally apply after Announcement Date.

New subsection 118.1(16) of the Act applies an ordering rule for the purpose of subsection 118.1(15) so that the acquisition of a non-qualifying security of a donor by a donee or the use of a donee's property by a donor will reduce the donor's charitable donations tax credits on a "first-in, first out" basis. For example, if in each of years 1 to 3 a donor makes a gift of $100 and in year 4 the donee acquires a non-qualifying security of the donor for $130, subsections 118.1(15) and (16) apply to eliminate the gift in year 1 and to reduce the gift in year 2 to $70. The gift in year 3 is not affected. This amendment applies after Announcement Date.

Clause 22

Medical Expense Tax Credit

ITA
118.2

Section 118.2 of the Act provides the medical expense tax credit.

Subclause 22(1)

ITA
118.2(2)(*b*.1)

Paragraph 118.2(2)(*b*.1) of the Act allows amounts paid as remuneration for part-time attendant care in Canada for an individual who has a severe and prolonged mental or physical impairment to qualify, up to a maximum of $5,000 ($10,000 if the individual has died in the year), as medical expenses, provided the amounts are paid to an attendant (other than the individual's spouse) who is at least 18 years of age and no other deduction is claimed in respect of those amounts. This amendment increases the $5,000 and $10,000 maximums to $10,000 and $20,000, respectively.

This amendment applies to 1997 and subsequent taxation years.

Subclause 22(2)

ITA
118.2(2)(*l*.4) to (*l*.7)

Subsection 118.2(2) of the Act lists the expenses that are considered qualifying medical expenses.

This amendment adds to the list of qualifying medical expenses the following four items:

- fees for sign language interpretation services provided to an individual who has a speech or hearing impairment, if the fees are paid to a person engaged in the business of providing such services;

- reasonable moving expenses (up to a maximum of $2,000) of an individual who lacks normal physical development or has a severe and prolonged mobility impairment to move to a dwelling that is more accessible by the individual or in which the individual is more mobile or functional;

- reasonable costs of alterations to the driveway of the principal place of residence of an individual who has a severe and prolonged

mobility impairment to facilitate the individual's access to a bus; and

- an amount (not in excess of $5,000) equal to 20% of the cost of a van that, at the time of its acquisition or within six months after that time, has been adapted for the transportation of an individual who requires the use of a wheelchair.

This amendment applies to 1997 and subsequent taxation years.

Subclause 22(3)

ITA
118.2(2)(*m*)

Under paragraph 118.2(2)(*m*) of the Act the cost of a device or of equipment may qualify as a medical expense if it is of a kind the Governor in Council has prescribed by regulation, having regard, where applicable, to the purpose of its acquisition or use. The amendment broadens the scope of the regulations by allowing the Governor in Council to stipulate a dollar limit for claims in respect of a particular device or equipment. The amendment is consequential on the inclusion, as a qualifying medical expense, of the cost (up to a maximum of $1,000) of an air conditioner to be used by an individual to cope with a severe chronic ailment, disease or disorder.

This amendment applies to 1997 and subsequent taxation years.

Clause 23

Disability Tax Credit

ITA
118.3(1)(*a*.2)

Subsection 118.3(1) of the Act provides the formula for calculating the disability tax credit and the conditions for entitlement to the credit for those individuals with a severe and prolonged mental or physical impairment. Only medical doctors (and, in the case of a sight impairment, optometrists) are allowed to certify impairments under

the existing Act. Under this amendment, audiologists will be authorized to certify a hearing impairment.

This amendment applies to certifications made after February 18, 1997.

Clause 24

Disability Tax Credit

ITA
118.4(2)

Subsection 118.4(2) of the Act defines a medical doctor, medical practitioner, dentist, pharmacist, nurse or optometrist as a person authorized to practice as such pursuant to provincial laws. This amendment, which is consequential on the amendment to paragraph 118.3(1)(*a*.2) of the Act, adds audiologists to the list of persons to whom subsection 118.4(2) applies.

This amendment applies after February 18, 1997.

Clause 25

Tuition Tax Credit

ITA
118.5(3)

Section 118.5 of the Act provides for a tax credit in respect of tuition fees paid to certain educational institutions. The amount of the credit is determined under subsection 118.5(1) by applying the appropriate percentage (17%) to the eligible fees paid for an individual's tuition to a qualified institution where the total of such fees exceeds $100. This amendment allows an individual to claim as tuition fees certain ancillary fees and charges (other than student association fees) paid in respect of the individual's enrolment at a post-secondary educational institution if the payment of such fees or charges is required from all of the institution's full-time students or part-time students, depending

on whether the individual is enrolled at the institution on a full-time or part-time basis.

Mandatory fees or charges do not qualify for the tuition tax credit to the extent that they are levied in relation to property to be acquired by students, services not ordinarily provided at post-secondary educational institutions in Canada or financial assistance to students. As well, mandatory charges paid by students to an educational institution for the construction or renovation of a building or facility generally do not qualify for the credit. An exception is made to the extent that the building or facility is owned by the institution and is used to provide courses at the post-secondary school level or services that, if fees or charges were required to be paid by all of the institution's students for such services, the fees or charges would be eligible for the tuition tax credit.

This amendment applies to the 1997 and subsequent taxation years.

Clause 26

Education Tax Credit

ITA
118.6(2)

Section 118.6 of the Act provides the education tax credit.

Subsection 118.6(2) of the Act contains the formula for calculating the amount of the credit. This amount is determined by multiplying the "appropriate percentage" (17%) by $100 and by the number of months in the year during which the individual was enroled as a full-time student in a qualifying education program at a designated educational institution. This amendment, which applies to 1997 and subsequent taxation years, increases the monthly amount used in the formula to calculate the credit from $100 to $150 for 1997 and to $200 thereafter.

Clause 27

Carryforward of Tuition and Education Tax Credits

ITA
118.61

New section 118.61 of the Act provides for the carryforward of a student's unused tuition and education tax credits.

Subsection 118.61(1) of the Act provides for the calculation of a student's unused tuition and education tax credits at the end of a taxation year that may be carried forward to future taxation years. That amount is determined by, first, adding to the student's unused tuition and education tax credits at the end of the previous year (where that year is after 1996) the portion of the student's tuition and education credits for the current year that is not needed to eliminate the student's tax payable for the current year. This total is then reduced by the amount of the tuition and education tax credits carryforward that is deductible for the year (which is, as set out in subsection 118.61(2), equal to the lesser of the previous year's carryforward and the tax that would be payable for the year by the student if no tuition and education tax credits were allowed). Finally, this total is further reduced by the tuition and education tax credits transferred for the year by the student to the student's spouse, parent or grandparent.

This amendment applies to 1997 and subsequent taxation years.

Clause 28

Transfer of Unused Credits to Spouse

ITA
118.8

Section 118.8 of the Act governs the transfer to a spouse of certain unused tax credits. The credits which may be transferred are the tuition and education tax credits and the age, pension and disability tax credits. The amendments to section 118.8 are consequential on the introduction of the carryforward of the tuition and education tax

credits under new section 118.61 of the Act. Starting with the 1997 taxation year, students will have the option of transferring the unused portion of their tuition and education tax credits or keeping it to reduce their own tax liability for future years. They will also be permitted to transfer part of the unused portion of these credits and carry forward the remainder.

This amendment applies to the 1997 and subsequent taxation years.

Clause 29

Transfer of the Tuition and Education Tax Credits

ITA
118.81

New section 118.81 of the Act provides for the calculation of the tuition and education tax credits that may be transferred for a taxation year from a student to the student's spouse under section 118.8 of the Act, or to a parent or grandparent under section 118.9 of the Act. The amount transferred is equal to the least of the three following amounts:

- the total of the student's tuition fee and education tax credits for the year,
- the amount for the year that the student designates in writing for the purpose of the transfer, and
- $850.

This amendment applies to 1997 and subsequent taxation years.

Clause 30

Transfers to Parent or Grandparent

ITA
118.9

Section 118.9 of the Act governs the transfer of a student's tuition and education tax credits to the student's parent or grandparent. The

amendment to section 118.9 is consequential on the introduction of the carryforward of the unused tuition and education tax credits under new section 118.61 of the Act. Starting with the 1997 taxation year, students will have the option of transferring the unused portion of their tuition and education tax credits or keeping it to reduce their own tax liability for future years. They will also be permitted to transfer part of the unused portion of these credits and carry forward the remainder.

This amendment applies to 1997 and subsequent taxation years.

Clause 31

Ordering of Credits

ITA
118.92

Section 118.92 of the Act provides that the tax credits allowed in computing any individual's tax payable are to be applied in a specific order. The amendment to this section adds a reference to section 118.61, which is the provision that allows for the carryforward of an individual's unused tuition and education tax credits under new section 118.61 of the Act.

This amendment applies to 1997 and subsequent taxation years.

Clause 32

Refundable Medical Expense Supplement

ITA
122.51

New section 122.51 of the Act provides a refundable tax credit for eligible individuals – the refundable medical expense supplement. The supplement is equal to the lesser of $500 and 25/17 of the medical expense tax credit claimed by an eligible individual for the year. The supplement is reduced by 5% of the individual's "adjusted income" in excess of an indexed threshold ($16,069 for 1997).

For the purpose of the new medical expense supplement, "eligible individual" for a taxation year is defined in subsection 122.51(1) as an individual (other than a trust) who is resident in Canada throughout the year, 18 years of age or older at the end of the year and whose total business and employment income (excluding disability benefits) for the year is at least $2,500. The individual's "adjusted income" for a taxation year is also defined under this subsection as being the total, for the year, of the individual's income and that of a spouse cohabiting with the individual at the end of the year.

Subsection 122.51(2) provides that an individual's medical expense supplement for a taxation year is deemed to be paid on account of the individual's tax liability for the year. Thus, to the extent that the supplement exceeds the individual's tax otherwise payable for the year, it will be refunded to the individual.

These amendments apply to 1997 and subsequent taxation years.

Clause 33

Investment Tax Credit

Subclauses 33(1) to (3)

ITA
127(9)

Subsection 127(9) of the Act provides definitions for terms that are used in the provisions relating to the investment tax credit.

"investment tax credit"

The definition of "investment tax credit" is amended to exclude expenditures in respect of which the taxpayer has not filed a prescribed form with Revenue Canada within one year after the taxpayer's filing-due date for the taxation year in which the expenditure was incurred. This requirement previously applied only to scientific research & experimental development investment tax credits.

This amendment applies to all taxation years, except that taxpayers who are not affected by the existing filing requirement in the definition of "qualified expenditure" in subsection 127(9) have until the date specified or May 31, 1997, whichever is later, to file the prescribed form.

"qualified expenditure"

The definition of "qualified expenditure" in subsection 127(9) of the Act is amended consequential on the amendment to the definition of "investment tax credit" to remove the filing requirement in paragraph (*e*), which now appears in the amended definition of "investment tax credit" as described in the commentary on that provision.

The definition is also amended to clarify that the reference to an expenditure incurred by the taxpayer in respect of scientific research and experimental development in amended paragraph (*f*) can apply to an expenditure described in subparagraph 37(1)(*a*)(i.1) of the Act. Expenditures described in that paragraph (generally non-arm's length payments for SR&ED) do not qualify as SR&ED expenditures for the purposes of calculating the investment tax credit of the payer. Rather, the SR&ED performer is entitled to claim SR&ED benefits on its expenditures or, in certain circumstances, renounce those expenditures in favour of the payer by way of a joint election under subsection 127(13).

The definition is further amended by moving the exception to the exclusion from "qualified expenditure" contained in paragraph (*g*) to the end of the paragraph, to clarify that an expenditure described in the first part of that paragraph, which is an expenditure on SR&ED directly undertaken by the taxpayer, is not excluded as a qualified expenditure.

These amendments apply to taxation years that begin after 1995.

"taxable supplier"

This definition is amended to correct a formatting error which arose between the initial release of the draft legislation introducing this provision and the tabling of the Notice of Ways and Means Motion containing the provision in December 1995. The concluding portion

"in the course of carrying on a business through a permanent establishment (as defined by regulation) in Canada" modifies both subparagraphs (*b*)(i) and (ii). This amendment applies to taxation years that begin after 1995.

Subclause 33(4)

ITA
127(11.4)

Subsection 127(11.4) of the Act was introduced contemporaneously with the introduction of the filing deadline for claiming SR&ED investment tax credits, to address the circumstances in which a taxpayer identified an amount as being a particular type of expense, but on reassessment Revenue Canada concluded that the amount should, instead, have been treated as SR&ED. In the absence of subsection 127(11.4), Revenue Canada could have been in the position of reassessing a taxpayer to disallow the classification made by the taxpayer, but also disallowing its classification as an SR&ED expense because it would be past the filing deadline.

In order to resolve this issue, subsection 127(11.4) of the existing Act provides that the filing deadline does not apply where Revenue Canada reclassifies an expenditure as SR&ED on an assessment of tax payable (or on a determination that no tax is owing). However, in order to ensure that taxpayers who do not file the required form on time are not accorded an inappropriate benefit because of a reassessment by Revenue Canada, subsection 127(11.4) is repealed for the 1997 and subsequent taxation years.

For the 1997 and subsequent taxation years, new subsection 37(12) of the Act will cause the affected expenditures to be treated, on an assessment by Revenue Canada, as if the SR&ED provisions did not exist. In most cases this will allow the taxpayer the original treatment claimed for the expenditure. Where that claim was also in error, Revenue Canada can assess to reflect the correct non-SR&ED classification of the expense.

As a transitional measure, subsection 127(11.4) is amended to refer to paragraph (*m*) of the definition "investment tax credit", consequential

on the introduction of the filing deadline in the definition "investment tax credit" applicable for the 1996 taxation year.

Clause 34

Qualifying Environmental Trust

ITA
127.41

Section 127.41 of the Act provides a refundable tax credit to beneficiaries of a mining reclamation trust.

Section 127.41 is amended so that the reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". This amendment is in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

This amendment applies to taxation years that end after February 18, 1997.

Clause 35

Minimum Tax

ITA
127.52(1)(*d*)(i)

Paragraph 127.52(1)(*d*) of the Act provides that in computing an individual's adjusted taxable income for minimum tax purposes the total amount of capital gains and losses is to be taken into account. This is achieved through the direction in the paragraph to ignore the references in sections 38 and 41 to "3/4 of". This amendment exempts from the application of this rule gains resulting from charitable donations and other gifts for which a charitable donations deduction or tax credit may be claimed. The result is that only the reduced amount of any such taxable capital gain will be included in

the base for determining an individual's minimum tax. This amendment applies to taxation years that begin after 1996.

Clause 36

Bankrupt Individuals

ITA
128(2)

Subsection 128(2) of the Act contains rules that apply to individuals who become bankrupt.

Subclause 36(1)

ITA
128(2)(*f*)

An individual who is bankrupt at any time in a taxation year is required under paragraph 128(2)(*f*) of the Act to file an income tax return for the year. This return is in addition to the return that is required under paragraph 128(2)(*e*) to be filed by the trustee in bankruptcy on behalf of the individual for the same taxation year. Paragraph 128(2)(*f*) is amended to deny the bankrupt individual a deduction under section 118.61 of the Act (carryforward of unused tuition and education tax credits). However, the trustee may claim a deduction under that section in the return filed under paragraph 128(2)(*e*). For further details on the carryforward of unused tuition and education tax credits, reference may be made to the commentary on section 118.61 of the Act.

This amendment applies to the 1997 and subsequent taxation years.

Subclause 36(2)

ITA
128(2)(*g*)

Paragraph 128(2)(*g*) of the existing Act prohibits an individual who is discharged absolutely from bankruptcy from deducting under section 111 losses carried forward from taxation years that ended

before the individual's discharge, as well as certain amounts in computing the individual's tax payable. Paragraph 128(2)(*g*) is amended to restrict the individual from deducting an amount under section 118.61 (carryforward of unused tuition and education tax credits) in respect of the individual's unused tuition and education tax credits at the end of the last taxation year that ended before the bankruptcy. For further details on the carryforward of unused tuition and education tax credits, reference may be made to the commentary on section 118.61 of the Act.

This amendment applies to the 1997 and subsequent taxation years.

Clause 37

Change of Residence

ITA
128.1(4)(*b*)(iii)

Subsection 128.1(4) of the Act provides a set of rules that apply to a taxpayer who ceases to be a resident of Canada. Under paragraph 128.1(4)(*b*), a taxpayer's property is generally treated in these circumstances as if it were disposed of at fair market value. Subparagraph 128.1(4)(*b*)(iii) provides an individual with an exemption from this deemed disposition where the property involved is a right to receive a pension benefit or certain other amounts described in subsection 212(1) in respect of which tax under Part XIII of the Act is payable by non-residents.

Subparagraph 128.1(4)(*b*)(iii) is amended to extend this exemption to rights under registered education savings plans.

This amendment applies after 1997.

Clause 38

Registered Retirement Savings Plans

ITA
146

Section 146 of the Act provides rules relating to registered retirement savings plans (RRSPs).

Subclause 38(1)

Registered Retirement Savings Plans

ITA
146(1)

"earned income"

Subsection 146(1) defines "earned income" which is relevant in determining the maximum deduction in respect of premiums under an RRSP.

This amendment to the English version of the definition "earned income" is consequential on the amendment to paragraph 56(8)(*a*). It ensures that, while all types of benefits received under the Canada and Quebec Pension Plans may be eligible for the special tax treatment provided under that paragraph, only disability pensions paid under those plans may be included in computing an individual's earned income for RRSP purposes.

This amendment applies to amounts received after 1995.

Subclauses 38(2) and (3)

ITA
146(1)

"RRSP deduction limit"

Subsection 146(1) of the Act defines "RRSP deduction limit", which is relevant in determining the maximum tax-deductible contributions that an individual may make for a year to RRSPs.

In general terms, an individual's RRSP deduction limit for a year is equal to the individual's unused deduction room carried forward from the previous year, *plus* any additional deduction room that becomes available in the year (based on the individual's earned income for the previous year and certain other factors), *minus* any deduction room used in the year as a consequence of past service improvements in post-1989 benefits under a registered pension plan (RPP).

The definition "RRSP deduction limit" is amended, for 1998 and subsequent taxation years, to add the amount of an individual's total pension adjustment reversal for a year to the individual's RRSP deduction limit for the year. An individual's total pension adjustment reversal for a year will be defined in the *Income Tax Regulations* as the sum of the individual's pension adjustment reversals (PARs) for the year under deferred profit sharing plans (DPSPs) and benefit provisions of RPPs.

The *Income Tax Regulations* will also be amended to provide rules for the calculation of PARs. Under those rules, the determination of an individual's PAR under a DPSP or benefit provision of an RPP will usually be required where the individual ceases, after 1996 and before retirement, to be entitled to benefits under the plan or provision. PAR will be included in the individual's total pension adjustment reversal for the year in which the individual's entitlement to benefits ceases (except where entitlement ceases in 1997, in which case the resulting PAR will be added to the individual's total pension adjustment reversal for 1998).

In general terms, the Regulations will define an individual's PAR under a defined benefit provision of an RPP to be the total of the individual's pension credits and past service pension adjustments

under the provision since 1990, *minus* any lump sum amounts paid to the individual, or transferred to an RRSP or other money purchase type of registered plan, in respect of the individual's post-1989 benefits under the provision. The Regulations will define an individual's PAR under a DPSP or money purchase provision of an RPP to be the total of all amounts included in the individual's pension credits under the plan or provision since 1990 but not vested in the individual.

The Regulations will generally require that an individual's PAR be reported to Revenue Canada and to the individual within 60 days after the calendar year quarter in which the individual ceases to be entitled to benefits under the DPSP or the benefit provision of the RPP, as the case may be. However, for those individuals who cease to be entitled to benefits after 1996 and before October 1998, the reporting deadline will be extended to December 31, 1998. The Regulations will require that PARs be reported by the plan administrator in the case of an RPP, and by the plan trustees in the case of a DPSP.

Draft amendments to the Regulations relating to PAR are to be released later this year.

Subclauses 38(3) and (4)

ITA
146(1)

"unused RRSP deduction room"

Subsection 146(1) of the Act defines "unused RRSP deduction room", which measures the amount of deduction room for RRSP contributions that an individual may carry forward from a year to use in future years.

In general terms, an individual's unused RRSP deduction room at the end of a year is equal to the individual's unused deduction room carried forward from the previous year, *plus* any additional deduction room that becomes available in the year (based on the individual's earned income for the previous year and certain other factors), *minus* the amount of any RRSP contributions deducted by the individual in computing income for the year and any deduction room used in the

year as a consequence of past service improvements in post-1989 benefits under a registered pension plan.

This definition is amended, for 1998 and subsequent taxation years, to include an individual's total pension adjustment reversal for a year in the calculation of the individual's unused RRSP deduction room at the end of the year. (See the commentary on the amendments to the definition "RRSP deduction limit" in subsection 146(1) of the Act for further information.)

Clause 39

Registered Education Savings Plans

ITA
146.1

Section 146.1 of the Act contains rules relating to registered education savings plans (RESPs). Significant amendments are being made to this section: to increase the annual contribution limit; to allow an RESP subscriber to receive the trust's accumulated income under certain circumstances; to permit RESP beneficiaries who are enroled in a distance education course to receive educational assistance payments; and to allow spouses to be joint subscribers under an RESP. Additional technical amendments are being made to improve the operation of the RESP rules.

Overview

The federal budget of February 18, 1997 announced significant changes to the rules governing registered education savings plans (RESPs). The purpose of this overview is to provide an outline of the existing rules governing RESPs, together with the proposed changes. For technical detail, reference should be made to proposed section 146.1 and Parts X.4 and X.5 of the Act and to the detailed explanatory notes with respect to those provisions. It must be stressed that, while the Act provides a basic framework for RESPs, the actual benefits provided under a specific RESP depend on its terms.

Q1. What are RESPs?

RESPs are vehicles designed for individuals to accumulate income for post-secondary education. Typically, the plans are entered into by parents seeking to save for their children's post-secondary education.

There are currently two basic types of RESPs. A qualifying child can be a beneficiary under a plan (sometimes referred to as a "group RESP") under which benefits are a proportionate share of income accumulating in respect of a group of children of the same age. In this case, contributions are made in respect of each such child under similar RESPs with the same promoter and the benefits for a child vary depending on the timing and amounts of contributions made in respect of the child and the investment performance of assets associated with the plan. A child or adult, alone or with family members, can also be a beneficiary under RESPs that are sometimes referred to as "self-directed" or "individual" RESPs.

An RESP is entered into between an RESP promoter and a subscriber. A subscriber can establish an RESP for the benefit of any number of beneficiaries. Where there is more than one beneficiary under a single plan, each beneficiary under the plan must be related to the subscriber by blood relationship or adoption. For example, an individual cannot establish an RESP for the individual's own benefit or the benefit of the individual's spouse unless there is only one beneficiary. However, a parent can establish an RESP for the benefit of all his or her children.

Q2. What are the contribution limits for RESPs?

The existing annual contribution limit per beneficiary is $2,000. The proposed amendments increase the $2,000 limit to $4,000 for 1997 and subsequent taxation years. The lifetime contribution limit per beneficiary remains at $42,000.

It should be noted that the contribution limits cannot be avoided by establishing more than one RESP or by having different subscribers establish RESPs. For example, if a grandparent contributed $1,500 into an RESP in respect of a grandchild in a year, the remaining RESP contribution room available to any other subscriber in respect of the grandchild in the year would be $2,500.

Q3. Can RESP income and RESP contributions be returned to a subscriber?

There is nothing in the Act which would prevent RESP contributions from being returned to a subscriber. Conversely, under the existing rules in the Act, RESP income cannot be returned to a subscriber, except by way of educational assistance payments. Educational assistance payments can generally be paid only to students in full-time attendance at a university or college, although the amendments will accommodate distance education by allowing such payments to be made to students taking a full-time course load at a university or college.

The amendments permit an RESP to make a distribution at any time after 1997 of accumulated income to a subscriber where the following conditions are met:

- the subscriber is resident in Canada,
- each beneficiary in respect of whom contributions were made by the subscriber has attained 21 years of age and is not eligible at that time to receive educational assistance payments, and
- the RESP has been in existence for at least 10 years.

After a subscriber's death, an RESP may allow for the distribution of accumulated income to any person resident in Canada. In addition, the "age 21" and "10 year hold" conditions are waived in the case of deceased beneficiaries.

It should also be noted that RESP assets can be transferred from one RESP to another without restarting the 10 year hold requirement.

Q4. What is the tax treatment of RESP contributions?

RESP contributions are not deductible in computing income. They can be returned to the subscriber at any time without tax consequences, in accordance with the terms of the RESP.

Q5. What is the tax treatment of RESP income?

RESP income is included in computing a recipient's income once it is distributed, and taxed accordingly. However, in many cases the recipient will be a student whose total income will result in a minimal amount of tax. The tax advantage of an RESP is that tax is not levied on an annual basis on undistributed RESP income.

When RESP income is returned to a subscriber under the new rules, an additional 20% tax is levied on the subscriber except to the extent that the subscriber "rolls over" the RESP income to an RRSP as described below. The 20% tax is in recognition of the deferral of taxes on interest and other income on funds contributed into an RESP. For example, assume $1,000 of RESP income is distributed to a subscriber whose marginal federal/provincial combined income tax rate is 50%, the subscriber will pay $500 of regular income tax and an additional $200 of penalty tax.

If, after the death of a subscriber, income is returned under the new rules to an individual other than the spouse or former spouse of the deceased subscriber, the 20% tax will apply with respect to such income.

Q6. Can the 20% penalty tax be avoided by transferring RESP income to an RRSP?

When RESP income is transferred on behalf of a subscriber into an RRSP, the RESP income is still included in computing the subscriber's income. However, the amount transferred into the RRSP counts as a normal RRSP contribution which can offset the income inclusion and eliminate the 20% penalty tax if the subscriber has sufficient unused RRSP room. Subject to a lifetime limit of $40,000, RESP income transferred into an RRSP will generally not be subject to the 20% penalty tax, provided that the subscriber deducts a regular RRSP contribution for the year of the transfer equal to at least the amount of the transfer. **Note: If a transfer of RESP income is made in the first 60 days of a taxation year, the 20% tax will be reduced only in the event that the transfer is deducted in computing income for that year.**

The proposed amendments will provide the authority to impose withholding taxes with respect to RESPs. However, to accommodate

transfers of RESP income to RRSPs, provision to waive withholding taxes will be made in some cases.

Q7. Can the 20% penalty tax also be avoided by transferring RESP income to a spousal RRSP of an RESP subscriber?

Yes, provided the RESP subscriber has sufficient RRSP deduction room.

Q8. What if the RESP contribution limits are exceeded?

Subscribers are required to report overcontributions in respect of a beneficiary, based on contributions to all plans in respect of the beneficiary. There is a 1% per month penalty tax in respect of excess amounts.

In addition, the registration of an RESP will become revocable in the event that an excess contribution is made in respect of a beneficiary. However, it is expected that the Minister of National Revenue would generally revoke a plan on this basis only in cases where there has been a flagrant disregard of the contribution limits.

Q9. What happens if an overcontribution to an RESP is made by mistake?

The Minister of National Revenue will have discretion to waive the penalty tax.

Q10. Can property be transferred from one RESP to another?

In most situations, a transfer from one RESP to another will not have any adverse consequences. Transfers can be made without any resulting taxes or penalties where there is a common beneficiary under the transferor and transferee plan. In addition, this rule will be extended to cases where a beneficiary under the transferor plan is a sibling of a beneficiary under the transferee plan, provided that the beneficiary under the transferee plan is under 21 years of age.

In situations not described above, transfers can result in penalty tax because the RESP contribution history in respect of each beneficiary under a transferor plan will, in effect, be assumed by each beneficiary under the transferee plan. As a consequence, each contribution that

was made into the transferor plan is treated on a retroactive basis as also having been made into the transferee plan.

Similar rules will also apply where one beneficiary replaces another beneficiary under the same plan.

Q11. Will RESPs have to be changed because of the proposed amendments to allow distributions of accumulated income?

No. On the other hand, the amendments will not prevent any change in the terms of existing RESPs. An existing arrangement could be altered where the parties to the arrangement agree. In addition, it is understood that "group" RESPs normally have specific contractual provisions governing modifications to existing arrangements.

ITA
146.1(1)

Subsection 146.1(1) of the Act defines a number of terms that apply to RESPs.

Subclause 39(1)

"pre-1972 income" and "tax-paid income"

These definitions are being repealed, effective after 1997. For further details, see the commentary on the repeal of subsections 146.1(8) to (10) of the Act.

Subclause 39(2)

"educational assistance payment"

An "educational assistance payment" is a payment, other than a refund of payments, made to a designated beneficiary under an education savings plan to assist the beneficiary to further his or her post-secondary education. Educational assistance payments are included in computing income under subsection 146.1(7). Paragraph 146.1(2)(*g*) and new paragraph 146.1(2)(*g*.1) are RESP registration rules which restrict the circumstances in which educational assistance payments can be made.

The definition is amended so that scholarships and other similar amounts paid out of an education savings plan to non-beneficiaries will also be treated as educational assistance payments. As indicated by existing paragraph (*b*) of the definition "trust" in subsection 146.1(1), payments of this nature to non-beneficiaries are contemplated under the RESP rules.

This amendment applies after 1997.

"education savings plan"

An RESP is an "education savings plan" that has been accepted for registration by the Minister of National Revenue. An "education savings plan" is defined as a contract between an individual who is the subscriber, and a person or organization who is the promoter. Under the terms of the contract, the subscriber makes contributions to the promoter in exchange for, among other things, the promoter's undertaking to make educational assistance payments to eligible beneficiaries.

The definition is amended to provide that the contract may be entered into jointly by an individual and the individual's spouse. It is also amended to prohibit a trust (which is treated as an individual for the purposes of the Act) from establishing an RESP. The existing reference to a "subscriber" within the definition has also been replaced by a new definition of "subscriber", which is explained in the commentary on that provision.

These amendments apply to contracts made after 1997.

"refund of payments"

A "refund of payments" under an education savings plan is essentially a return of all or part of the contributions made by or on behalf of a subscriber under the plan.

The definition is amended to clarify that a "refund of payments" under a plan also includes an amount transferred from another plan to the extent that the amount would have been a "refund of payments" if it had been paid directly to a subscriber under the other plan.

This amendment applies to 1997 and subsequent taxation years.

"registered education savings plan"

A "registered education savings plan" is an education savings plan that has been accepted for registration by Revenue Canada.

The definition is amended so that an RESP that is amended subsequent to registration continues to be considered to be an RESP. The definition is also amended to provide that, once the registration of an education savings plan has been revoked under amended subsection 146.1(13), the plan is no longer treated as an RESP (except for the purposes of the income inclusion rules in subsections 146.1(7) and (7.1) and the overcontribution tax in Part X.4 of the Act). This exception ensures that educational assistance payments and accumulated income payments made under a revoked plan will be included in the recipient's income.

These amendments apply after 1997.

Subclause 39(3)

"trust"

For the purpose of the RESP rules, a "trust" is defined to be any person who irrevocably holds property pursuant to an education savings plan for a number of limited purposes. Under paragraph (*b*) of the definition, one of the permitted purposes of an RESP trust is the payment of scholarships to non-beneficiaries.

Paragraph (*b*) of the definition is being eliminated. This amendment is consequential on an amendment to the definition "educational assistance payment", under which payments of scholarships and other amounts to non-beneficiaries will be treated as educational assistance payments. For further detail, see the commentary on the amendments to the definition "educational assistance payment".

The definition is also amended so that after 1997 a trust is permitted to provide for the payment of accumulated income payments. For further details, see the commentary on the new definition of "accumulated income payment".

These amendments apply after 1997.

Subclause 39(4)

"accumulated income payment"

The definition "accumulated income payment" is being introduced, effective after 1997. It is any distribution out of an education savings plan, other than a distribution that is an educational assistance payment, a refund of payments, a payment to an educational institution in Canada or a transfer to another RESP.

Accumulated income payments are required under new subsection 146.1(7.1) of the Act to be included in computing the recipient's income and are relevant in computing the special 20% tax in new Part X.5 of the Act. The circumstances in which such payments can be made is limited by new paragraph 146.1(2)(*d*.1).

"RESP annual limit"

The definition "RESP annual limit" is introduced, effective after 1989. It represents the maximum annual amount that can be contributed to an RESP in a year in respect of a beneficiary. The amount was $1,500 from 1990 to 1995 and $2,000 for 1996 and will be $4,000 for 1997 and subsequent years. The definition is used in amended paragraph 146.1(2)(*k*) and amended Part X.4 of the Act.

"subscriber"

The existing definition "subscriber", contained within the definition of "education savings plan", defines a subscriber simply as the individual who entered into the RESP contract with the promoter.

A separate definition of "subscriber" is being introduced, effective for contracts entered into after 1997. Generally, a subscriber under an education savings plan is the individual (or individuals) with whom the promoter entered into the plan. The definition also provides for replacement subscribers under certain circumstances relating to marriage breakdown and death, as described below.

Where a spouse or former spouse of a subscriber acquires the subscriber's rights under the plan pursuant to a court order or written agreement relating to a division of property between the two individuals on the breakdown of their marriage, the spouse or former

spouse is considered to be a subscriber under the plan. In such a case, the former subscriber ceases to be a subscriber under the plan.

Also, where the plan allows a person to make contributions into the plan after the death of a subscriber, the person is a subscriber under the plan. For example, if the estate of the subscriber continues to make contributions into the plan in respect of the plan's beneficiaries, the estate is considered to be a subscriber.

The definition is relevant for a number of purposes. Under new paragraph 146.1(2)(*d*.1), an RESP may allow a subscriber to receive "accumulated income payments". Under amended Part X.4 of the Act, the liability for RESP overcontributions tax is imposed on RESP subscribers.

Subclause 39(5)

ITA
146.1(2)

Subsection 146.1(2) of the Act sets out the requirements that must be satisfied in order to register an education savings plan. The preamble to subsection 146.1(2) is amended to make it clear that the requirements in that subsection do not simply relate to the terms of an education savings plan. This amendment is, in part, consequential on the amendment to paragraph 146.1(2)(*m*) described in the commentary below.

This amendment applies to applications made after 1997. Other amendments to subsection 146.1(2) are described in the commentary below.

ITA
146.1(2)(*b*)

Paragraph 146.1(2)(*b*) of the Act requires that, before an education savings plan may be registered, there must be at least 150 subscribers who have entered into plans with the promoter which meet all the other requirements of subsection 146.1(2). Note, however, that relief from this requirement is provided under subsection 146.1(3).

Paragraph 146.1(2)(*b*) is amended by changing the requirement that there be at least 150 subscribers who have entered into plans with the promoter to a requirement that there be at least 150 plans entered into with the promoter. Paragraph 146.1(2)(*b*) is also amended to eliminate an unnecessary reference to the former Act.

These amendments apply to applications made after 1997.

Subclause 39(7)

ITA
146.1(2)(*d*) and (*d*.1)

Paragraph 146.1(2)(*d*) of the Act ensures that payments to a subscriber under a plan are restricted to a refund of payments (unless the subscriber is also the beneficiary under the plan). Under the existing rules, subscribers generally forfeit RESP income in the event the designated beneficiaries do not pursue post-secondary education.

Paragraph 146.1(2)(*d*) is amended so that the restriction applies only to payments made to a subscriber under a plan before 1998. This amendment is consequential on the introduction of new paragraph 146.1(2)(*d*.1) of the Act which permits RESP income to be returned to a subscriber where certain conditions are satisfied.

New paragraph 146.1(2)(*d*.1) is added to allow, but not require, RESPs to be established or amended so that subscribers (and other persons) can receive RESP income under certain circumstances. An RESP may provide after 1997 for the payment of "accumulated income payments" (as defined in subsection 146.1(1)) to or on behalf of a person resident in Canada. Generally, the person must be a subscriber under the plan. However, where a subscriber has died, the plan may allow accumulated income payments to be made to any person resident in Canada.

Where more than one person is entitled to receive accumulated income payments under a plan, the payments must be made separately to each person. The plan must not allow for the payments to be made jointly.

In addition, the following conditions must be satisfied at the time an accumulated income payment is made:

- each individual in respect of whom a contribution had been made into the plan has attained 21 years of age and is not pursuing post-secondary education (or each such individual is deceased); and

- the plan has been in existence for at least 10 years (or each individual in respect of whom a contribution had been made into the plan is deceased and was the subscriber, was related to a subscriber, or was the nephew, niece, great nephew or great niece of a subscriber).

New subsection 146.1(7.1) requires the inclusion in income of accumulated income payments received under an RESP. In addition, new Part X.5 of the Act sets out a special tax on accumulated income payments.

These amendments apply to 1998 and subsequent taxation years.

ITA
146.1(2)(*g*) and (*g*.1)

Paragraph 146.1(2)(*g*) of the Act provides that educational assistance payments to beneficiaries of RESPs may be made only where the beneficiary is a student in full-time attendance at a post-secondary institution and enroled in a qualifying educational program.

Paragraph 146.1(2)(*g*) is amended so that it applies only with respect to payments made before 1997. This amendment is consequential on the introduction of new paragraph 146.1(2)(*g*.1).

New paragraph 146.1(2)(*g*.1) provides that educational assistance payments made after 1996 to an individual under an RESP may be made only where the individual is enroled in a qualifying educational program as a full-time student at a post-secondary educational institution. As a result, educational assistance payments may now be made out of an RESP to students who are taking distance education courses, such as correspondence courses.

Amended paragraph 146.1(2)(*g*) and new paragraph 146.1(2)(*g*.1) apply to plans entered into after February 20, 1990. However, for plans entered into before 1998, the restrictions do not apply to students who are not designated RESP beneficiaries.

ITA
146.1(2)(*g*.2)

New paragraph 146.1(2)(*g*.2) of the Act requires that each contribution made into an RESP either be a subscriber contribution made in respect of a beneficiary under the plan, or a transfer from another RESP.

This amendment applies to 1997 and subsequent taxation years.

Subclause 39(9)

ITA
146.1(2)(*i*.1)

New paragraph 146.1(2)(*i*.1) of the Act applies only with respect to an RESP that allows for the payment of accumulated income payments. Where a plan allows such payments, the plan must provide for its termination on or before March of the year following the year in which the first such payment is made.

This amendment applies to 1998 and subsequent taxation years.

ITA
146.1(2)(*i*.2)

New paragraph 146.1(2)(*i*.2) of the Act prohibits a plan from receiving property from another RESP after the other plan has made an accumulated income payment. This condition ensures that transfers between plans cannot be used to extend the life of a plan beyond the term provided for in new paragraph 146.1(2)(*i*.1).

This amendment applies to 1998 and subsequent taxation years.

Subclause 39(10)

ITA
146.1(2)(*j*)

Paragraph 146.1(2)(*j*) of the Act restricts the selection of RESP beneficiaries, where a plan permits more than one individual to be a beneficiary. Where this is the case, the subscriber must be connected

by blood relationship or adoption to each of the beneficiaries. Subsection 251(6) provides rules for determining connection by blood relationship and adoption.

Paragraph 146.1(2)(*j*) is amended to ensure that this restriction operates as intended where an RESP has more than one subscriber. Where this is the case and there is more than one beneficiary, each of the beneficiaries must be connected by blood relationship or adoption to each of the living subscribers (or to have been connected to a deceased original subscriber). This amendment relates to an amendment to the definition "education savings plan" in subsection 146.1(1), which contemplates an RESP having joint subscribers.

Subparagraph 146.1(2)(*j*)(ii) is introduced to restrict the contributions that can be made in respect of a beneficiary, in the event that an RESP allows more than one beneficiary. A contribution into the plan in respect of a beneficiary in these circumstances is permitted to be made only where:

- the beneficiary has not attained 21 years of age at the time the plan was entered into, or

- the contribution is made by way of a transfer from another RESP or after such a contribution, provided that another contribution in respect of the beneficiary had been made before the transfer into the other plan.

While special provision is made above for transfers from another RESP, new paragraph 146.1(2)(*g*.2) does not allow a plan to accept contributions into the plan by way of a transfer from another education savings plan in the event that the registration of the other plan has been revoked. The registration of the other plan will be revocable under subsections 146.1(12.1) to (13) in the event that the other plan does not comply with new subparagraph 146.1(2)(*j*)(ii).

These amendments generally apply to 1998 and subsequent taxation years. However, the whole of paragraph 146.1(2)(*j*) does not apply to plans entered into before July 14, 1990. In addition, subparagraph 146.1(2)(*j*)(ii) does not apply to plans entered into before 1998.

Subclause 39(11)

ITA
146.1(2)(*k*)

Paragraph 146.1(2)(*k*) of the Act ensures that an RESP will not accept contributions in respect of a beneficiary which exceed $2,000 per year.

Paragraph 146.1(2)(*k*) is amended to raise this limit to the RESP annual limit. As defined in subsection 146.1(1), the RESP annual limit for the 1997 and subsequent years is $4,000.

Paragraph 146.1(2)(*k*) is also amended so that, for the purpose of this paragraph, contributions made by way of a transfer from another RESP do not use up this limit. Note, however, that RESP overcontributions may result in a penalty tax for the subscriber under Part X.4 of the Act.

These amendments apply to plans entered into after February 20, 1990.

Subclause 39(12)

ITA
146.1(2)(*m*)

Paragraph 146.1(2)(*m*) of the Act requires that an RESP comply with prescribed conditions. There are no conditions currently prescribed for this purpose.

Paragraph 146.1(2)(*m*) is replaced by a further condition for registration of an education savings plan. For an education savings plan to be accepted for registration, the Minister of National Revenue must have no reasonable basis to believe that the promoter will not take all reasonable measures to ensure that the plan will continue to comply with the plan registration conditions.

This amendment applies to applications made after 1997.

Subclause 39(13)

ITA
146.1(4.1)

New subsection 146.1(4.1) of the Act applies where an RESP is amended. It requires the promoter to file the text of the amendment with Revenue Canada within 60 days after the plan is amended. The penalty for failure to comply with this requirement is provided under subsection 162(7) of the Act.

The requirement to file RESP amendments does not apply until Royal Assent. However, Revenue Canada currently requires, in paragraph 27 of Information Circular 93-3, that amendments be submitted.

Subclause 39(14)

ITA
146.1(6.1)(*a*)

Subsection 146.1(6.1) of the Act contains special rules that apply with respect to transfers of property from one RESP to another.

Paragraph 146.1(6.1)(*a*) ensures that RESP transfers will not result in penalty tax under Part X.4 of the Act. Paragraph 146.1(6)(*a*) is repealed, effective for transfers that occur after 1996. This amendment is consequential on the introduction of subsection 204.9(5) of the Act.

Subclause 39(15)

ITA
146.1(6.1)(*b*) and (*c*)

Paragraph 146.1(6.1)(*b*) of the Act ensures that transfers from one RESP to another cannot be used to avoid specified registration conditions. It provides that, for the purposes of paragraphs 146.1(2)(*h*) and (*i*), the transferee plan is deemed to have been entered into on the earlier of the day otherwise determined and the day on which the transferor plan was entered into.

Paragraph 146.1(6.1)(*b*) is amended so that this deeming rule also applies for the purpose of new subparagraph 146.1(2)(*d.*1)(vi) of the Act, which generally prohibits distributions of RESP accumulated income from plans that have existed for less than 10 years. This ensures that property can be transferred from one RESP to another without restarting the "10 year hold" requirement. Amended paragraph 146.1(6.1)(*b*) applies after 1997.

New paragraph 146.1(6.1)(*c*) of the Act, which applies to transfers that occur after 1997, exempts transferred amounts from being included in computing the income of any person.

Subclause 39(16)

ITA
146.1(7)

Subsection 146.1(7) of the Act requires that an RESP beneficiary include in income for a taxation year the total of all educational assistance payments paid to, or on behalf of, the beneficiary in the year under the plan, excluding the beneficiary's portion of "tax-paid-income".

Subsection 146.1(7) is amended so that educational assistance payments paid out of an RESP to or for any individual are included in computing the individual's income. This ensures that non-beneficiaries who receive scholarships under the plan are required to include such amounts in computing their income.
Subsection 146.1(7) is also amended to delete the provisions relating to "tax-paid-income" as they are no longer relevant. For further details, see the commentary on subsections 146.1(8) to (10) of the Act.

These amendments apply to 1998 and subsequent taxation years.

ITA
146.1(7.1) and (7.2)

New subsection 146.1(7.1) of the Act provides that accumulated income payments received by a taxpayer in a taxation year under an RESP are required to be included in computing the taxpayer's income for the year.

In order to discourage the trading of RESP interests, subsection 146.1(7.1) also provides that any amounts received by a taxpayer in a year from the disposition of a subscriber's interest under an RESP, other than amounts excluded by virtue of new subsection 146.1(7.2), are included in the taxpayer's income for the year. For this purpose, the following amounts are excluded:

- any amount received under the plan;
- any amount received in satisfaction of a right to a refund of payments; and
- any amount received under a court order or written agreement relating to a division of property between two individuals on the breakdown of their marriage.

These amendments apply to 1998 and subsequent taxation years.

Subclause 39(17)

ITA
146.1(8) to (10)

Subsections 146.1(8) to (10) of the Act contain income exclusion rules that apply with respect to the distribution of property relating to pre-1972 income of a trust governed by an education savings plan. To the extent that trust income earned prior to 1972 had been included in the subscriber's income, the rules provide a deduction for the portion of "tax-paid-income" included in payments to a beneficiary under the plan.

Subsections 146.1(8) to (10) are repealed for 1998 and subsequent taxation years as they are no longer relevant, since all pre-1972 plans would be expected to have been wound up by this time.

Subclause 39(18)

ITA
146.1(12.1) to (13)

Subsection 146.1(13) of the Act permits the Minister of National Revenue to revoke the registration of an RESP that ceases to comply

with the requirements for registration. The existing rules are amended to improve the procedure for revoking the registration of an RESP. The new rules are similar to those found in section 147.1 of the Act that apply to the revocation of the registration of a pension plan.

New subsection 146.1(12.1) of the Act provides that the Minister may revoke the registration of an RESP if:

- the plan ceases to comply with the conditions for its registration;
- the plan ceases to comply with any provision of the plan; or
- an individual has become liable for tax under Part X.4 of the Act because of contributions into the plan.

As a first step in revoking the registration of an RESP, the Minister must notify the promoter in writing of the Minister's intention to revoke the plan's registration as of a specified day. The day can be no earlier than the day of the failure that entitles the Minister to send the notice of intent, or the last day of the month for which tax under Part X.4 of the Act is payable, as the case may be. Upon receipt of such a notice, the promoter under the plan may, under amended subsection 172(3) of the Act, appeal to the Federal Court of Appeal.

New subsection 146.1(12.2) provides that, after the Minister has sent a notice of intent to revoke the registration of an RESP, the Minister may notify the promoter in writing that the registration of the plan is revoked as of a specified date, which day can be no earlier than the day stated in the notice of intent. The notice of revocation cannot be sent until 30 days after the notice of intent was sent.

Amended subsection 146.1(13) provides that the registration of an RESP is revoked as of the day specified in the Minister's notice of revocation sent under subsection 146.1(12.2) unless, in the course of an appeal under subsection 172(3), the Federal Court of Appeal orders otherwise.

These amendments apply after 1997.

Subclause 39(19)

ITA
146.1(14)

A trust governed by a revoked RESP is subject to tax under Part I of the Act on its taxable income. Any distributions from the revoked RESP as educational assistance payments or accumulated income payments are required to be included in the recipient's income pursuant to subsections 146.1(7) and (7.1) of the Act. In addition, distributions from a revoked RESP may give rise to penalty tax under new Part X.5 of the Act. Existing subsection 146.1(14) provides for an amount to be included in computing the income of a subscriber upon the revocation of an RESP.

Subsection 146.1(14) is being repealed, effective after 1997. It is no longer considered necessary in light of the other tax implications described above with respect to revoked RESPs.

Subclause 39(20)

ITA
146.1(15)

New subsection 146.1(15) of the Act allows the Governor in Council to make regulations requiring promoters to file information returns relating to education savings plans.

This amendment applies on Royal Assent.

Clause 40

Registered Pension Plans

ITA
147.1(18)

Paragraph 147.1(18)(*d*) of the Act allows the Governor in Council to make regulations requiring registered pension plan administrators to make determinations relating to the computation of pension adjustments and past service pension adjustments. This paragraph is

amended to include, after 1996, a reference to pension adjustment reversals.

Paragraph 147.1(18)(*t*) of the Act allows the Governor in Council to make regulations defining several expressions used in the Act, such as "pension adjustment" and "past service pension adjustment". This paragraph is amended to include, after 1996, a reference to "total pension adjustment reversal".

See the commentary on the amendments to the definition "RRSP deduction limit" in subsection 146(1) of the Act for further information.

Clause 41

RPP Transfers

ITA
147.3(14.1)

Existing subsections 147.3(9) to (11) of the Act set out the tax consequences associated with transfers between registered pension plans (RPPs) and transfers from an RPP to a registered retirement savings plan or to a registered retirement income fund. With the introduction of new subsection 147.3(14.1), subsections 147.3(9) to (11) are also made to apply to transfers between benefit provisions of the same RPP.

Specifically, new subsection 147.3(14.1) provides that, where property held under one benefit provision of an RPP is made available to pay benefits under another benefit provision of the same plan, subsections 147.3(9) to (11) apply in the same manner as they would have applied if the provisions had been in separate RPPs.

This means that, where an amount is transferred on behalf of an individual from one benefit provision to another of the same RPP and the transfer is not in accordance with any of subsections 147.3(1) to (7) of the Act, the amount is deemed to have been paid from the plan to the individual and, as such, is taxable. The amount is also deemed to have been paid by the individual to the plan as a contribution under the recipient provision.

It should be noted that, by virtue of subsection 147.3(14) read in conjunction with subsection 147.3(14.1), subsections 147.3(9) to (11) also apply where property held under one benefit provision is made available to pay benefits under another benefit provision of the same RPP without the property being actually transferred.

New subsection 147.3(14.1) applies to transactions occurring on or after Announcement Date.

Clause 42

Exemptions from Tax

ITA
149(1)(*z*)

Paragraph 149(1)(*z*) of the Act exempts mining reclamation trusts from tax under Part I of the Act. Instead, these trusts are taxed under Part XII.4.

Paragraph 149(1)(*z*) is amended so that the reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". This amendment is in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

This amendment applies to the 1997 and subsequent taxation years.

Clause 43

Assessment

ITA
152

Section 152 of the Act contains rules relating to assessments and reassessments of tax, interest and penalties payable by a taxpayer and to determinations of amounts of tax deemed to have been paid by a taxpayer.

Subclause 43(1)

ITA
152(1)(*b*)

Subsection 152(1) of the Act lists certain refunds and deemed payments of tax that are to be determined by Revenue Canada in the course of assessing a taxpayer's tax return.

Paragraph 152(1)(*b*) refers to the specific provisions of the Act under which amounts are deemed to be paid on account of tax. The amendment to this paragraph adds a reference to subsection 122.51(2) which is the provision under which the new refundable medical expense supplement is granted. The amendment also deletes obsolete references.

This amendment generally applies to 1997 and subsequent taxation years.

Subclauses 43(2) and (3)

Assessments

ITA
152(4) and (4.01)

Generally, Revenue Canada may not reassess tax payable by a taxpayer for a taxation year after the expiry of the normal reassessment period for the year. Paragraph 152(4)(*b*) of the Act, however, sets out four cases in which Revenue Canada may make reassessments up to three years after the normal reassessment period. New subparagraph 152(4)(*b*)(v) is added to the Act to permit Revenue Canada to make such reassessments where they are required by the rules in new subsections 118.1(14) and (15) relating to charitable donations. For further information, reference may be made to the commentary on those provisions.

Subsection 152(4.01) of the Act limits the matters in respect of which Revenue Canada may reassess, where a reassessment is made after the normal reassessment period. New subparagraph 152(4.01)(*b*)(v) is added to the Act to apply when a reassessment is made under new subparagraph 152(4)(*b*)(v) in order to give effect to new

subsection 118.1(14) or (15). This amendment allows the reassessment to be made only to the extent that it relates to one of those subsections.

These amendments apply after Announcement Date.

Subclause 43(4)

ITA
152(4.2)(*d*)

Subsection 152(4.2) of the Act gives Revenue Canada discretion to make a reassessment or a redetermination beyond the normal reassessment period when so requested by a taxpayer who is an individual or a testamentary trust in order to give the taxpayer a refund or to reduce taxes payable. The amendment to paragraph 152(4.2)(*d*) adds a reference to subsection 122.51(2) to enable Revenue Canada to make a redetermination of the new refundable medical expense supplement. The amendment also deletes obsolete references.

These amendments apply to 1997 and subsequent taxation years.

Clause 44

Withholding of Tax

ITA
153(1)

Subsection 153(1) of the Act authorizes regulations for the withholding of tax from the payments described in paragraphs 153(1)(*a*) to (*r*).

Paragraph 153(1)(*s*) is added to authorize the withholding of tax from payments under registered education savings plans.

This amendment applies to payments made after 1997.

Clause 45

Instalment Payments

ITA
156.1(1)

Subsection 156.1(1) of the Act sets out definitions that are relevant for the purpose of determining whether relief from tax instalments is available under subsection 156.1(2) or (4) of the Act. The definition "net tax owing" is amended so that tax payable under new Part X.5 of the Act is treated the same as tax under Part I of the Act for this purpose. This amendment applies to 1998 and subsequent taxation years.

Clause 46

False Statements or Omissions

ITA
163(2)(*c*.2)

Subsections 163(2) of the Act imposes a penalty where a taxpayer, knowingly or in circumstances amounting to gross negligence, participates in or makes a false statement or omission in a return, form, certificate, statement or answer. The amendment to paragraph 163(2)(*c*.2) is consequential on the introduction of the refundable medical expense supplement. It also deletes references to section 126.1 of the Act, which have become obsolete.

This amendment applies to 1997 and subsequent taxation years.

Clause 47

Appeals

ITA
172(3)

Subsection 172(3) of the Act provides a taxpayer with a right of appeal to the Federal Court of Appeal where the Minister of National Revenue takes a number of actions, including refusing to accept an education savings plan for registration under section 146.1 or revoking the registration of such a plan under subsection 146.1(13). The time limit for instituting the appeal is set out in subsection 180(1) of the Act.

Subsection 172(3) is amended so that the right of appeal in respect of a revocation arises because of the sending of a notice of intent to revoke under new subsection 146.1(12.1), rather than because of the revocation itself.

This amendment applies after 1997.

Clause 48

Appeal Period

ITA
180(1)

Subsection 180(1) of the Act sets out the deadline for instituting an appeal to the Federal Court of Appeal after the Minister of National Revenue has taken an action that gives rise to a right of appeal under subsection 172(3). The deadline is 30 days after the date of such action, with provision for the extension of the deadline by the Court.

Subsection 180(1) is amended so that the same deadline also applies with respect to the right of appeal arising from a notice of intent to revoke the registration of a registered education savings plan.

This amendment applies after 1997.

Clause 49

Tax on Capital of Financial Institutions - Calculation

ITA
190.1

Part VI of the Act levies a tax on the taxable capital employed in Canada of financial institutions. In general terms, a financial institution's taxable capital employed in Canada is the amount of its long-term debt, equity and non-deductible reserves that are considered to be used in connection with its activities carried on in Canada.

ITA
190.1(1.2)

Subsection 190.1(1.2) of the Act imposes an additional temporary Part VI tax on the taxable capital employed in Canada of financial institutions, other than life insurance corporations. The additional tax is equal to 0.15% of the corporation's taxable capital employed in Canada in excess of its "enhanced capital deduction" of $400 million. Where the corporation is related to another financial institution at the end of the year, the enhanced capital deduction must be shared by members of the related group.

The additional tax, which was introduced in the 1995 budget and extended in the 1996 budget, is scheduled to expire on October 31, 1997. This amendment extends the application of the additional tax until October 31, 1998. For taxation years that include October 31, 1998, the additional tax will be prorated on the basis of the number of days in the taxation year that are before November 1, 1998.

This amendment applies to taxation years that end after February 27, 1995.

Clause 50

Cumulative excess amount in respect of RRSPs

ITA
204.2(1.1)(*b*)

Subsection 204.1(2.1) of the Act imposes a penalty tax in respect of excess contributions made after 1990 to registered retirement savings plans (RRSPs). The amount of tax payable in respect of any month is 1% of an individual's cumulative excess amount at the end of that month.

Subsection 204.2(1.1) of the Act defines an individual's cumulative excess amount at the end of any month in a year to be the excess of the individual's undeducted RRSP premiums at that time over the amount determined by the formula in paragraph 204.2(1.1)(*b*). Generally, the amount determined by the formula is the amount of RRSP deduction room available to the individual for the year *plus* a margin of $2,000.

The formula in paragraph 204.2(1.1)(*b*) is amended, for the 1998 and subsequent taxation years, to add an amount (variable R) which is the individual's total pension adjustment reversal for the year. (See the commentary on the amendments to the definition "RRSP deduction limit" in subsection 146(1) of the Act for further information.)

Clause 51

Labour-Sponsored Venture Capital Corporations

ITA
204.8 to 204.87

Part X.3 of the Act imposes various taxes and penalties on labour-sponsored venture capital corporations (LSVCCs) registered under that Part. A tax credit is provided under section 127.4 of the Act in respect of the acquisition of shares issued by LSVCCs.

Part X.3 is retitled so that it now refers to all LSVCCs, rather than simply those registered under Part X.3. This change is made because

of the introduction of new subsections 204.82(5), 204.83(2) and 204.85(2), which apply to LSVCCs not registered under Part X.3.

This amendment applies after February 18, 1997.

Clause 52

Labour-Sponsored Venture Capital Corporations - Definitions

ITA
204.8

"eligible investment"

Section 204.8 of the Act defines terms for the purposes of Part X.3 of the Act.

An "eligible investment" of an LSVCC generally includes a share or debt issued by an eligible business entity where, immediately after the issue of the share or debt, the following three conditions are satisfied:

- the LSVCC's total investment in the eligible entity (and all corporations related to the entity) is not more than 10% of the LSVCC's shareholders' equity and not more than $10 million;

- the carrying value of the total assets of the eligible entity and all corporations related to it does not exceed $50 million; and

- the number of employees of the eligible entity and all corporations related to it does not exceed 500.

The definition is amended so that the $10 million limit is increased to $15 million.

The definition is also amended so that the last two conditions are applied immediately before the issue of the share or debt by the eligible entity, rather than immediately after.

The definition is also amended so that a prescribed LSVCC that is related to the eligible entity is ignored for the purpose of the second condition. It is intended that section 6701 of the *Income Tax*

Regulations will be amended to add a cross reference to the definition.

The definition is also amended so that only one-half of the number of employees normally working less than 20 hours per week is taken into account for the purpose of determining whether the 500 employee limit is satisfied.

These amendments apply to property acquired after February 18, 1997.

Clause 53

Labour-Sponsored Venture Capital Corporations - Conditions

ITA
204.81(1)(*c*)(ii)(C)

Subsection 204.81(1) of the Act permits Revenue Canada to register a corporation as an LSVCC under Part X.3 of the Act if its articles satisfy specified conditions and other requirements are met. Clause 204.81(1)(*c*)(ii)(C) sets out the conditions that must be met for an LSVCC to issue additional classes of shares, apart from class A shares issued to individuals and class B shares issued to a labour body. Under this clause, an LSVCC may generally issue only additional classes of shares without voting rights and only if the Minister of Finance approves the shares.

Clause 204.81(1)(*c*)(ii)(C) is amended so that voting rights may be attached to additional classes of shares that can be issued by an LSVCC.

This amendment applies after 1996.

Clause 54

Labour-Sponsored Venture Capital Corporations - Recovery of Credit

ITA
204.82(2) to (2.2)

Subsection 204.82(2) of the Act imposes a tax on an LSVCC that was registered under Part X.3 where, at any time after the fifth taxation year of the LSVCC ending after it first issues Class A shares, it fails to meet a required level of eligible investment. This level, at any time in a particular taxation year, is 60% of the lesser of the LSVCC's shareholders' equity at the end of the preceding taxation year and the LSVCC's shareholders' equity determined at the end of the LSVCC's current taxation year (in both cases determined without taking into account any unrealized gains or losses on the LSVCC's eligible investments). If there is an investment shortfall at any time in the month, the LSVCC is required to pay a tax in respect of the month equal to the greatest such shortfall in the month multiplied by 1/60 of the prescribed rate of interest in effect for the month. Investment shortfalls in 12 consecutive months result in larger taxes and penalties (representing a recovery of federal LSVCC tax credits) applying under subsections 204.82(3) and (4) of the Act.

Subsection 204.82(2) is being split into three subsections (subsections 204.82(2) to (2.2)), in order to reflect a number of policy changes. The liability for tax is established under subsection 204.82(2). The investment shortfall on which the tax is based is now calculated under subsections 204.82(2.1) and (2.2). In addition, there are five substantive changes being made to the rules that are currently contained in subsection 204.82(2).

The first and second changes are of a technical nature. Amended subsection 204.82(2) makes it clear that the tax under that subsection for a taxation year applies only in respect of months that end in the year. In addition, the investment shortfall for a month that straddles a taxation year is determined with reference to the greatest investment shortfall in the portion of the month that is in the year.

The third change is meant to accommodate LSVCCs that increase their level of small business investment during a taxation year,

effectively imposing the required investment level on a more gradual basis. To the extent that an LSVCC's total average cost of eligible investments in a taxation year exceeds the LSVCC's total cost of eligible investments at the time the investment shortfall is being calculated, under new paragraph (*b*) of the description of variable B in subsection 204.82(2.1), the excess will reduce the LSVCC's shortfall at that time. The average total cost for a taxation year is determined solely with reference to costs at the beginning and at the end of the year. This amendment applies to taxation years that end after 1998.

The fourth change is of a tightening nature and is intended to ensure that the minimum general holding period for Class A shares corresponds with the length of time during which the capital raised by such shares is required to be used to acquire eligible investments. Under subsection 211.8(1) of the Act, the general holding period is effectively 8 years for shares acquired after March 5, 1996 and 5 years for shares acquired on or before that date. The change is reflected in paragraphs 204.82(2.2)(*b*) and (*c*), which are rules that apply for the purpose of computing an LSVCC's investment shortfall.

Under these paragraphs, an LSVCC's shareholders' equity at the end of a taxation year must now generally be determined without reference to redemptions of Class A shares that are expected to occur after the end of the year. However, there is an exception for each redemption that occurs in the first 60 days of the following year, provided that tax under Part XII.5 of the Act became payable as a consequence of the redemption (or the redemption would have been exempt from Part XII.5 tax if it had occurred at the end of the earlier year.) These paragraphs apply for the purpose of computing investment shortfalls in taxation years that end after 1998, except that the percentage of expected redemptions that is ignored is 20% for the 1999 taxation year, 40% for the 2000 taxation year, 60% for the 2001 taxation year and 80% for the 2002 taxation year. This transitional rule allows LSVCCs time to make any necessary increases in their levels of eligible investments.

The last change is meant to encourage investments in smaller businesses, which for this purpose are defined as businesses which do not exceed a $10 million asset limit (rather than the $50 million limit otherwise applicable under the definition "eligible investment" in section 204.8). Under new paragraph 204.82(2.2)(*d*), the cost of each

eligible investment in such a business is grossed-up by 50% for the purpose of calculating an LSVCC's investment shortfall at any time, provided the investment was made after February 18, 1997.

Except as noted above, these amendments apply to taxation years that end after February 1997.

ITA
204.82(5)

Subsection 204.82(5) of the Act imposes a new tax under Part X.3 of the Act on LSVCCs that have been prescribed under the *Income Tax Regulations* for the purpose of the definition "approved share" in subsection 127.4(1) and that were not registered under Part X.3.

If such an LSVCC is liable to pay an amount to the government of a province as a consequence of a failure to acquire sufficient properties (i.e., small business properties) of a character described in the law of the province, the LSVCC is generally liable to pay a tax under Part X.3 for the taxation year in which that amount became payable equal to that amount. However, this new subsection does not require the matching of provincially-imposed interest on unpaid provincial amounts payable. Instead, because of section 204.87, interest on unpaid Part X.3 tax will be calculated in accordance with rules under Part I of the Act.

Subsection 204.82(5) also does not apply to any amount payable under or as a consequence of a prescribed provision of the law of the province. It is intended that Part LXVII of the Regulations will be amended to provide a list of prescribed provisions for this purpose. Section 25.1 of the Ontario Labour-Sponsored Venture Capital Corporations Act, which imposes special additional penalties on provincially-registered LSVCCs for the failure to meet provincial investment requirements in respect of certain small businesses, will be included in this list. At this time, no other prescribed provision is contemplated.

In accordance with new subsection 204.86(2), such an LSVCC must file a return under Part X.3 for the taxation year in which tax becomes payable under subsection 204.82(5). The tax is payable within 90 days after the end of the taxation year in which the liability arose.

This amendment applies to liabilities arising after February 18, 1997.

Clause 55

Labour-Sponsored Venture Capital Corporations - Refund of Tax and Penalty

ITA
204.83

Section 204.83 of the Act provides that Revenue Canada must refund 100% of the tax payable by an LSVCC under subsection 204.82(3) and 80% of the penalty payable by it under subsection 204.82(4) where, throughout any 12 month period beginning after the 12 month period in respect of which the tax became payable, it has maintained the required level of eligible investments.

Existing section 204.83 is renumbered as subsection 204.83(1), as a consequence of the introduction of new subsection 204.83(2).

Subsection 204.83(2) is introduced to provide a further refund mechanism, as a consequence of the introduction of subsection 204.82(5) which imposes Part X.3 tax on certain provincially-registered LSVCCs. The refund is available to such an LSVCC where:

- the government of a province refunds, at any time, an amount to the LSVCC;

- the refund is of an amount that had been paid in satisfaction of a particular amount payable in a taxation year of the LSVCC; and

- tax was payable under subsection 204.82(5) by the LSVCC for a taxation year because the particular amount became payable.

In these circumstances, the LSVCC is, at that time, deemed to have paid an amount on account of its Part X.3 tax payable for that year equal to the amount of the refund.

This amendment applies after February 18, 1997.

Clause 56

Labour-Sponsored Venture Capital Corporations - Restrictions on Dissolution

ITA
204.85

Section 204.85 of the Act provides that a federally-registered LSVCC (including a revoked corporation) may not liquidate or dissolve without the written permission of the Minister of Finance, if the federally-registered LSVCC has issued Class A shares. The Minister of Finance also has the authority to impose terms and conditions upon dissolution of such corporations.

Existing section 204.85 is renumbered as subsection 204.85(1), as a consequence of the introduction of subsection 204.85(2). Section 204.85 is also amended to provide that, after Announcement Date, a federally-registered LSVCC may not be amalgamated or merged with another corporation without the written permission of the Minister of Finance.

New subsection 204.85(2) imposes a tax on LSVCCs that have been prescribed for the purpose of the definition "approved share" in subsection 127.4(1) but which are not federally-registered LSVCCs.

This tax is imposed where an amount is payable after February 18, 1997 to the government of a province by an LSVCC as a consequence of the amalgamation or merger of the LSVCC with another corporation, the winding-up or dissolution of the LSVCC or the LSVCC ceasing to be registered under the law of the province. The LSVCC is generally liable to pay a tax under Part X.3 of the Act for the taxation year in which the amount became payable to the province equal to that amount. However, this measure does not require the matching of provincially-imposed interest on unpaid provincial amounts payable. Instead, because of section 204.87, interest on unpaid Part X.3 tax will be calculated in accordance with rules under Part I of the Act. In addition, this measure does not apply to any amount payable under or as a consequence of any provision of the law of the province that is prescribed under Part LXVII of the *Income Tax Regulations*. At this time, no prescribed provision is contemplated.

In accordance with new subsection 204.86(2), an LSVCC must file a return under Part X.3 for the taxation year in which tax becomes payable under subsection 204.85(2). The tax is payable within 90 days after the end of the taxation year in which the liability arose.

Clause 57

Labour-Sponsored Venture Capital Corporations - Return and Payment of Tax

ITA
204.86

Section 204.86 of the Act provides that every federally-registered LSVCC (including revoked corporations) must file an annual return under Part X.3 of the Act.

Existing section 204.86 is renumbered as subsection 204.86(1), as a consequence of the introduction of new subsection 204.86(2).

The effect of new subsection 204.86(2) is described in the commentary on new subsections 204.82(5) and 204.85(2) of the Act.

These amendments apply to taxation years that end after February 18, 1997.

Clause 58

Tax in Respect of Overpayment to Registered Education Savings Plans

ITA
Part X.4
204.9

Part X.4 of the Act provides for a special tax to be paid by subscribers with respect to overcontributions made to registered education savings plans (RESPs).

Part X.4 is amended to reflect the increase in the annual contribution limit in respect of RESP beneficiaries for 1997 and subsequent years. It is also amended to allow the replacement after 1996 of a beneficiary under an RESP by a brother or sister of the beneficiary who is under 21 years of age, generally without penalty tax implications. Part X.4 is also amended to allow Revenue Canada to waive Part X.4 tax where appropriate. Finally, a number of technical changes have been made to improve the operation of this tax.

It should also be noted that, under new subsections 146.1(12.1) to (13), Revenue Canada may revoke the registration of an RESP where a subscriber under the plan is liable for Part X.4 tax because of overcontributions under the plan. However, it is expected that Revenue Canada would generally revoke the registration of a plan on this basis only where there has been a flagrant disregard of the contribution limits.

The following commentary explains the amendments to Part X.4 in greater detail.

Subclause 58(1)

ITA
204.9(1)

Definitions

Subsection 204.9(1) defines a number of expressions used in Part X.4.

An "excess amount" for a year in respect of a beneficiary under an RESP is the total amount on which tax is payable under Part X.4. An excess amount arises when the total of all contributions made into RESPs for a particular beneficiary either exceeds the annual limit of $2,000 in any year, or causes the lifetime contribution limit of $42,000 to be exceeded.

The definition "excess amount" is amended, for 1997 and subsequent years, to raise the $2,000 annual limit to the "RESP annual limit". As defined in subsection 146.1(1) of the Act, the RESP annual limit for 1997 and subsequent years is $4,000. The definition is further

amended to refer to the new expression "RESP lifetime limit", rather than $42,000.

The definition "RESP lifetime limit" is introduced to simplify the description of "excess amount". The lifetime limit is $31,500 for 1990 to 1995, and $42,000 for 1996 and subsequent years.

The definition "subscriber's gross cumulative excess" is introduced for the purpose of determining a subscriber's liability for Part X.4 tax. A "subscriber's gross cumulative excess" is the total of all amounts each of which is the "subscriber's share of the excess amount" for a particular year in respect of a beneficiary. The "subscriber's share of the excess amount" is essentially the subscriber's pro-rata share of any RESP overcontributions made in respect of a particular beneficiary. The new definition, which applies for determining Part X.4 tax for months after 1996, is added for technical clarity and does not reflect any change of policy to Part X.4.

Subclause 58(2)

ITA
204.9(4) and (5)

Designation of New Beneficiaries

Paragraph 204.9(4)(*a*) of the existing Act contains an anti-avoidance rule that applies when a beneficiary under an RESP is replaced by another. The rule provides that the contributions previously made into the plan for the former beneficiary are considered to have been made for the new beneficiary. This is intended to ensure that the contribution limits are not multiplied by having a number of plans for different beneficiaries and changing the beneficiary designation just prior to terminating the plans. This existing rule, subject to the amendment described below and changes made for technical clarity, has been maintained under amended subsection 204.9(4).

Amended subsection 204.9(4) also, after 1996, allows an individual under 21 years of age to replace a brother or sister as a beneficiary under an RESP, without penalty tax implications. The contributions that were previously made in respect of the former beneficiary are not

taken into account in determining RESP overcontributions or unused limits with regard to the new beneficiary.

To ensure that amended subsection 204.9(4) does not result in excessive penalty tax, new paragraph 204.9(4)(*c*) deems the contributions that were made in respect of the former beneficiary to have been withdrawn at the time of the replacement. Therefore, to the extent that overcontributions were previously made in respect of the former beneficiary, the overcontributions are only taken into account in computing Part X.4 tax in respect of the new beneficiary.

These amendments apply to replacements of beneficiaries that occur after 1996.

Transfers between RESPs

The existing rules with respect to RESP transfers in paragraph 146.1(6.1)(*a*) and 204.9(4)(*b*) have been replaced by new subsection 204.9(5).

Subsection 204.9(5) continues, in modified form, the mechanism for allowing property to be transferred from one RESP to another. Where there has been such a transfer, under paragraph 204.9(5)(*a*) the amount transferred is deemed not to have been contributed into the transferee plan except as provided by paragraph 204.9(5)(*b*) and (*c*).

Paragraph 204.9(5)(*c*) ensures that, in most situations, a transfer from one RESP to another will not have any adverse tax consequences. Transfers after 1996 can be made without resulting in any penalty tax under Part X.4 in two cases:

- there is a common beneficiary under the transferor plan and the transferee plan; or

- a beneficiary under the transferor plan is a sibling of a beneficiary under the transferee plan, provided that the beneficiary under the transferee plan is under 21 years of age.

Except for the two cases described above, transfers can result in penalty tax because of the anti-avoidance rule in paragraph 204.9(5)(*b*). This rule, which is similar to the rule in paragraph 204.9(4)(*a*), is intended to ensure that RESP transfers are

not used as a means of multiplying a beneficiary's contribution limits. It provides that the contributions that were previously made by a subscriber into the transferor plan are deemed to have been made by the subscriber in respect of each of the beneficiaries under the transferee plan at the time those earlier contributions were made. In other words, the contribution history in respect of each beneficiary under the transferor plan is, in effect, assumed by each beneficiary under the transferee plan.

In the two cases described above, paragraph 204.9(5)(*d*) provides that the amount transferred is deemed not to have been withdrawn from the transferor plan. This rule is intended to ensure that a distribution from an RESP by way of transfer to another RESP does not in itself reduce Part X.4 tax.

In addition, paragraph 204.9(5)(*e*) provides that each subscriber under the transferor plan is deemed to be a subscriber under the transferee plan. This rule is intended to prevent a subscriber from transferring overcontributions to an RESP that has a different subscriber as a means of circumventing Part X.4 tax. It ensures that the subscriber under the transferor plan remains liable for any Part X.4 tax resulting from the overcontributions.

New subsection 204.9(5) applies to transfers that occur after 1996.

Clause 59

Tax Payable by Subscribers

ITA
204.91

Calculation of Part X.4 Tax

Under the existing rules in section 204.91 of the Act, the penalty tax is equal to 1% per month on the subscriber's share of the excess amount in respect of a beneficiary to the extent that the share has not been withdrawn.

The method for determining the amount of tax payable in respect of RESP overcontributions is being modified for technical clarity.

Under new subsection 204.91(1), the tax is equal to 1% of the amount by which the total of all of the subscriber's gross cumulative excesses (determined at the end of the month) in respect of beneficiaries exceeds the total of such excesses that have been withdrawn from RESPs.

New subsection 204.91(1) applies in computing tax under Part X.4 for months after 1996.

Special Rules

New subsection 204.91(2) of the Act allows Revenue Canada to waive Part X.4 tax where it is just and equitable to do so, having regard to all factors (including a number of factors specifically mentioned in the subsection). This amendment applies from the time of the introduction of Part X.4 (after January 1990).

New subsection 204.91(3) applies where a spouse or former spouse of a subscriber under an RESP has, because of a division of property on marriage breakdown, acquired the subscriber's rights under the plan. In such a case, for the purpose of determining Part X.4 tax for months after 1997 that are after the acquisition of such rights, all previous contributions made into the plan by the former subscriber are deemed to have been made by the subscriber's spouse or former spouse. The purpose of this rule is to ensure that the spouse who has control over the operation of an RESP is liable for Part X.4 tax in respect of the RESP arising after marriage breakdown.

New subsection 204.91(4) ensures that, after the death of a subscriber of an RESP, the estate of the subscriber becomes liable for any Part X.4 tax in respect of the RESP for months after the death. New subsection 204.91(4) applies for the purpose of determining Part X.4 tax for months after 1997.

Clause 60

Special Tax on Income Payments from Registered Education Savings Plans

ITA
Part X.5
204.94

New Part X.5 of the Act sets out a special 20% tax on "accumulated income payments" from RESPs. This tax can generally be reduced to the extent that the recipient of such a payment makes deductible RRSP contributions under subsection 146(5) or (5.1) of the Act for the year in which the payment is made. The purpose of this tax is to discourage the use of RESPs strictly for their tax deferral advantages, particularly in regard to individuals who already maximize the tax advantages for retirement savings that are associated with RRSPs.

Subsection 204.94(1) of the Act provides that the meanings given to terms in subsection 146.1(1) also apply for the purposes of new Part X.5. The key definition is "accumulated income payment", which is essentially any distribution from an RESP that is not an educational assistance payment or a refund of payments. The definition "subscriber", which is modified for the purposes of Part X.5 to exclude persons who are subscribers by virtue of paragraph (*c*) of that definition, is also relevant. For further details on the definitions, see the commentary on amended section 146.1.

The base on which the 20% Part X.5 tax is charged for a person under subsection 204.94(2) is the sum of two amounts (designated as variables A and B), minus a third amount (designated as variable C).

Variable A is the total of all accumulated income payments made from an RESP under which the person is a subscriber (or, where there is no subscriber, a surviving spouse of a deceased subscriber), to the extent that the payments are included in computing the person's income for the year. For this purpose, subsection 204.94(1) provides that a "subscriber" does not include a person who becomes a subscriber under the plan after the death of a subscriber.

Variable B is the total of all accumulated income payments made from an RESP or a revoked plan, to the extent that the payments are

included in computing the person's income for the year and are not included in the value of A.

Variable C is an offset. The maximum offset is equal to the lesser of the value of A and the amounts deducted under subsections 146(5) and (5.1) in computing the taxpayer's income for the year. In addition, there is a $40,000 lifetime limit on the RRSP deductions that can be used to reduce the Part X.5 tax.

The effect of the formula is that only those individuals who received accumulated income payments that are included in the value of A can transfer the payments to an RRSP to minimize Part X.5 tax. This means that the RRSP transfer option is available only to:

- an original subscriber under the plan;

- a subscriber under the plan who is a spouse or former spouse of a former subscriber under the plan and who acquired the former subscriber's rights as a consequence of marriage breakdown; and

- a spouse or former spouse of a deceased subscriber, but only where there is no subscriber under the plan.

The example below illustrates the computation of Part X.5 tax.

EXAMPLE

The RESP under which Marie is an original subscriber permits accumulated income payments. Marie receives $14,000 of such payments in January 1999, of which $5,000 is directly transferred to an RRSP under which Marie is the annuitant. Marie claims a $4,000 RRSP deduction under subsection 146(5) for the 1998 taxation year and a $1,000 deduction for the 1999 taxation year.

Results:

1. The value of A is $14,000. The value of C is $1,000 (i.e., the $4,000 deduction claimed for 1998 is irrelevant).

2. Consequently, the tax under Part X.5 is $2,600 (20% x (14,000 - 1,000)).

3. In order to have reduced Part X.5 tax further, Marie should have refrained from deducting RRSP contributions for the 1998 taxation year.

Subsection 204.94(3) provides that a person liable for Part X.5 tax must file a return on or before the person's tax return filing-due date for the year. Unpaid Part X.5 tax for a year must be remitted to Revenue Canada by that date. Under subsection 204.94(4), administrative rules in Part I of the Act also apply for the purposes of Part X.5.

These amendments apply to 1998 and subsequent taxation years.

Clauses 61 and 62

Tax on Qualifying Environmental Trusts

ITA
Part XII.4
211.6

Part XII.4 of the Act imposes a special tax on mining reclamation trusts, as defined under subsection 248(1).

Part XII.4 is amended so that each reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". This amendment is in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

Part XII.4 is also amended so that the deadlines referred to in subsection 211.6(3) and (4) of the Act for filing the Part XII.4 tax return for a taxation year and paying Part XII.4 tax for the year are now referred to as the trust's "filing-due date" and "balance-due day" for the year, respectively. (Each such deadline for a taxation year is 90 days after the end of the year.) This amendment does not reflect any change in policy.

These amendments apply to the 1997 and subsequent taxation years.

Clause 63

Non-Resident Withholding Tax

ITA
212(1)(*r*)

Paragraph 212(1)(*r*) of the Act provides for non-resident withholding tax under Part XIII of the Act with respect to payments received from registered education savings plan, to the extent that those payments are required to be included in computing income under section 146.1 of the Act.

Paragraph 212(1)(*r*) is amended to ensure that amounts included in computing the non-resident person's taxable income or taxable income earned in Canada are not subject to Part XIII withholding tax.

This amendment applies to amounts paid or credited after February 28, 1979.

Clause 64

Non-Residents – Deemed Payments

ITA
214(3)(*j*)

Under subsection 214(3) of the Act, certain amounts that would, if a non-resident person were resident in Canada, be required to be included in the person's income are treated, for the purpose of the non-resident withholding tax, as payments to the person. Paragraph 214(3)(*j*) applies with respect to amounts that are required to be included in computing income of a subscriber under a registered education savings plan by virtue of subsection 146.1(14).

Paragraph 214(3)(*j*) is being repealed, effective after 1997, consequential on the repeal of subsection 146.1(14).

Clause 65

Release of Taxpayer Information

ITA
241(3.2)

Section 241 of the Act prohibits the communication or use by government officials of information obtained in administering the income tax system, except as authorized by that section. New subsection 241(3.2) permits Revenue Canada to release specified information relating to a charity that was at any time registered under the Act. This information includes the charity's governing documents, the names of its directors and other information relating to the registration of the charity and, if applicable, the revocation of its registration. This information may be released following enactment of this amendment.

Clause 66

Definitions

ITA
248(1)

Subsection 248(1) of the Act defines a number of terms that apply for purposes of the Act.

"cost amount"

Subsection 248(1) of the Act defines "cost amount". The cost amount of an interest of a beneficiary under a mining reclamation trust is considered to be nil.

The definition is amended so that the reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". This amendment is in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in this subsection. For more details, see the commentary on that definition.

This amendment applies after 1995.

"private foundation"
"public foundation"

The definitions of "private foundation" and "public foundation", which relate to the rules in the Act on charitable organizations, are provided in subsection 149.1(1). Subsection 248(1) is amended to incorporate those definitions for all purposes of the Act. These amendments apply after 1996.

"qualifying environmental trust"
"mining reclamation trust"

Subsection 248(1) of the Act defines the expression "mining reclamation trust". It is generally a trust maintained for the sole purpose of funding the reclamation of a mine in the province in which the trust is resident. The expression is used in paragraphs 12(1)(*z*.1) and (*z*.2), 20(1)(*ss*) and (*tt*) and 75(3)(*c*.1), sections 107.3 and 127.41, Part XII.4 and subsection 250(7), all of which affect the taxation of mining reclamation trusts and their beneficiaries.

The definition "mining reclamation trust" is being repealed, with effect after 1997. All "mining reclamation trusts" will now instead become "qualifying environmental trusts". The existing rules for mining reclamation trusts now apply to qualifying environmental trusts.

The sole purpose of a "qualifying environmental trust" must now be for funding the reclamation of a site in Canada that had been used primarily for, or for any combination of, the operation of a mine, the extraction of clay, peat, sand, shale or aggregates (including dimension stone and gravel) or the deposit of waste. There is no longer any restriction in the definition (as there was under paragraph (*b*) of the definition "mining reclamation trust") that would prevent such funding being used in connection with the reclamation of a clay pit, peat deposit, gravel pit, peat bog, sand pit or stone quarry.

The broader aspects of the definition "qualifying environmental trust" (as compared with the definition "mining reclamation trust") apply to

a trust where the first contribution to the trust was made after 1995, no distributions from the trust were made before February 19, 1997 and no interest in the trust was disposed of before February 19, 1997. However, a trust may elect under paragraph (*i*) of the definition never to have been a "qualifying environmental trust" if, before 1998 or April of the year following the year in which the first contribution to the trust was made, the trust files an election to this effect with Revenue Canada. Such an election also results in a trust losing any status that it might otherwise have as a mining reclamation trust. Revenue Canada has authority to reassess any taxpayer before 2000 in order to give effect to this election.

The introduction of the definition "qualifying environmental trust" applies after 1991, although the broader aspects of the definition will result in a deduction only for taxation years that end after February 18, 1997. For further detail, see the commentary on amended paragraph 20(1)(*ss*) of the Act under which the deduction for contributions to qualifying environmental trusts is provided.

"total pension adjustment reversal"

Subsection 248(1) of the Act is amended to add, after 1996, the definition "total pension adjustment reversal". This expression is defined to have the meaning assigned by regulation. (See the commentary on the amendments to the definition "RRSP deduction limit" in subsection 146(1) of the Act for further information.)

Clause 67

Residence of a Qualifying Environmental Trust

ITA
250(7)

Subsection 250(7) of the Act applies for the purposes of determining the province in which certain trusts reside. It applies where a trust resident in Canada would be a "mining reclamation trust", as defined by subsection 248(1), if it were resident in the province in which the mine to which the trust relates is situated. Where this is the case, the trust is considered to be resident in that province and not in any other province.

Subsection 250(7) is amended so that the reference to a "mining reclamation trust" is replaced by a broader reference to a "qualifying environmental trust". Similarly, reference to a "mine" is replaced by a broader reference to a "site". These amendments are in consequence of the extension of the rules for mining reclamation trusts reflected by the new definition "qualifying environmental trust" in subsection 248(1). For more details, see the commentary on that definition.

This amendment applies after 1995.

PART II

EXPLANATORY NOTES TO DRAFT AMENDMENTS ANNUITY CONTRACTS AS QUALIFIED INVESTMENTS FOR RRSPs AND RRIFs

Division A

Clause 68

Transfer of Refund of Premium under RRSP

ITA
60(*l*)

An individual is generally required to include in income any amount received out of a deferred income plan, such as a registered retirement savings plan (RRSP) or registered retirement income fund (RRIF). However, if the amount received is an amount described in subparagraph 60(*l*)(v) of the *Income Tax Act*, the individual can claim an offsetting deduction under paragraph 60(*l*) up to the lesser of the amount received and the total of any qualifying payments made by the individual. A qualifying payment is a payment made into an RRSP or a RRIF or a payment made to acquire an annuity contract described in subparagraph 60(*l*)(ii).

Three types of annuity contract are described in subparagraph 60(*l*)(ii). Each one has either a term or guaranteed period that is determined by reference to the age of the taxpayer making the qualifying payment or of the taxpayer's spouse. Subparagraph 60(*l*)(ii) is amended to clarify that the relevant age in each case is the age in whole years of the relevant person at the time that the annuity is acquired.

Subparagraph 60(*l*)(ii) is also amended to clarify the length of the guaranteed period in the case of a life annuity described in clause 60(*l*)(ii)(A). Where an annuitant is married, the length of this period cannot exceed 90 years minus the lesser of the age of the annuitant and the age of the annuitant's spouse.

These amendments, which apply to 1989 and subsequent taxation years, make the wording of subparagraph 60(*l*)(ii) consistent with the wording of new paragraph (*c*.1) of the definition "qualified investment" in subsection 146(1) of the Act.

Clause 69

Registered Retirement Savings Plans

ITA
146(1)

"qualified investment"

The definition "qualified investment" in subsection 146(1) of the Act sets out the types of property that a trust governed by a registered retirement savings plan (RRSP) is permitted to hold. If a trust governed by an RRSP acquires or holds a property that is not a qualified investment, there are generally unfavourable tax consequences for the RRSP annuitant under subsection 146(10) or the trust under Part XI.1 of the Act.

Paragraph (*c*) of the definition provides that an annuity contract that could have been purchased directly as an RRSP by an RRSP annuitant is a qualified investment for a trust governed by an RRSP. For this paragraph to apply, it is expected that an annuity contract would specify that payments must ultimately be made directly to the RRSP annuitant and not to the trust.

Paragraph (*c*) of the definition is amended by replacing some of the existing words in the paragraph with the expression "licensed annuities provider". The latter expression is now defined in amended subsection 248(1) of the Act, as described in the commentary below. This amendment does not represent a change in policy.

New paragraph (*c*.1) permits another type of annuity contract to be a "qualified investment" for a trusteed RRSP, provided that the annuity contract satisfies two conditions:

- the RRSP trust must be the only person that has the right to receive any annuity payments under the contract (unless the trust disposes of the annuity); and

- the annuity contract must give the holder of the contract an ongoing right to surrender the contract for an amount that, ignoring reasonable sales and administrative charges, approximates the amount that could be required to fund the future periodic payments under the contract.

Paragraph (*c*.1) is intended to allow an RRSP trust to hold various types of accumulation annuities and segregated fund policies. In addition, a deferred annuity under which periodic payments have begun can continue to be a "qualified investment" under paragraph (*c*.1), if the holder has a right to surrender the contract after the payments begin.

New paragraph (*c*.2) of the definition allows a third type of annuity contract to qualify as an investment for an RRSP trust, provided that the annuity meets the following six conditions:

- (1) periodic payments under the annuity contract are required to be made on an annual or more frequent basis;

- (2) the RRSP trust must be the only person that has the right to receive any annuity payments under the contract (unless the trust disposes of the annuity);

- (3) neither the time nor the amount of any payment under the contract can vary because of the length of any life, other than the life of the RRSP annuitant;

- (4) the date on which the periodic payments began or are to begin must be no later than the end of the year in which the RRSP annuitant attains 70 years of age;

- (5) the annuity contract must be either

    (a) a life annuity for the life of the RRSP annuitant that does not have a guaranteed period that runs past the end of the year in which the RRSP annuitant attains 90 years of age, except that where the RRSP annuitant had a spouse at the time that the

contract was acquired, the guaranteed period, if any, can run up to the end of the year in which the spouse attains 90 years of age (if that is a later year), or

(b) a term annuity with a term equal to either 90 years minus the age of the RRSP annuitant at the date on which the periodic payments start or 90 years minus the age of the RRSP annuitant's spouse as of that date; and

- (6) the periodic payments must be equal unless

(a) they have been adjusted for reasons that would, if the contract were an annuity under a retirement savings plan, be in accordance with the indexing or other options provided under subparagraphs 146(3)(*b*)(iii) to (v) of the Act, or

(b) they have been uniformly reduced as a consequence of a partial surrender of the right to receive periodic payments under the contract.

Paragraph (*c*.2) is intended to permit an RRSP trust to hold an annuity that is similar to an annuity described in paragraph (*c*), except that the annuity can be in pay before the RRSP's maturity date and be paid to the RRSP trust. Paragraph (*c*.2) does not permit an RRSP trust to hold a life annuity for the joint lives of the RRSP annuitant and the RRSP annuitant's spouse, in order to avoid possible valuation problems on the death of the RRSP annuitant.

These amendments apply after 1996. Similar amendments have also been made to the definition "qualified investment" in subsection 146.3(1) of the Act which applies with respect to registered retirement income funds.

Subclause 69(2)

Life Insurance Policies – Annuity Contracts

ITA
146(11.1)

Provisions incorporated by reference in subsection 146(11) of the Act deem the acquisition of a life insurance policy by an RRSP trust not to be the acquisition of a "non-qualified investment" in certain cases. When subsection 146(11) was enacted, the Act did not define the term "life insurance policy" and the term took its ordinary meaning, which did not include an annuity contract. However, the term "life insurance policy" was subsequently defined in subsections 138(12) and 248(1) to include an annuity contract and no consequential amendment was made to subsection 146(11). Accordingly, subsection 146(11) may permit an RRSP trust to acquire and hold an annuity contract in some cases.

Subsection 146(11.1) is introduced to provide that subsection 146(11) does not apply to annuity contracts issued after 1997. Instead, paragraph (*c*) and new paragraphs (*c*.1) and (*c*.2) of the definition "qualified investment" in subsection 146(1) expressly set out the types of annuity contracts which are qualified investments for trusteed RRSPs.

Clause 70

Registered Retirement Income Funds

ITA
146.3(1)

Subsection 146.3(1) of the Act defines a number of terms for the purposes of the rules governing registered retirement income funds (RRIFs) in section 146.3.

"minimum amount"

Each year, the carrier of a retirement income fund must generally pay to the annuitant not less than a prescribed fraction of the fair market

value of the property held in connection with the fund at the beginning of the year. The required payment is determined under the definition "minimum amount". The fraction is prescribed in section 7308 of the *Income Tax Regulations*.

The amendments to the definition "minimum amount" are largely consequential on new paragraphs (*b*.1) and (*b*.2) of the definition "qualified investment". As described below, these paragraphs permit a trusteed RRIF to hold certain types of annuity contracts. For convenience, an annuity described in new paragraph (*b*.2) (other than a commutable annuity described in new paragraph (*b*.1)) is referred to below as a "locked-in annuity".

As a consequence of these amendments, the "minimum amount" for the year under an RRIF is now the total of:

- the prescribed fraction for the year multiplied by the total fair market value of properties (other than locked-in annuities) held in connection with the fund at the beginning of the year, and

- the total of all amounts each of which is either a periodic payment received by the trust in the year under a locked-in annuity or an estimate of a periodic payment the trust would have received under a locked-in annuity held at the start of the year if it had not disposed of the right to the payment during the year.

These amendments avoid the difficulty of determining the fair market value of a locked-in annuity each year and make it practical for a minimum amount to be calculated and distributed where a locked-in annuity is held by an RRIF trust. If an RRIF trust holds only locked-in annuities at the beginning of a year, the minimum amount for the year under the RRIF will never exceed the annuity payments received by the trust in that year.

These amendments also ensure that the carrier of an RRIF will not have to pay out any more in a given year with respect to a locked-in annuity than would be paid under an RRSP annuity acquired to provide a retirement income on the maturity of an RRSP. This is appropriate, given that locked-in annuities are very similar to the types of annuities that can be acquired to provide a retirement income on the maturity of an RRSP.

The definition of "minimum amount" is also amended so that the prescribed fraction, referred to above, is referred to in the definition as a prescribed factor, rather than a prescribed amount. This change has been made for technical clarity, as the expression "amount" in the Act is generally reserved for amounts of a monetary nature. Corresponding changes to section 7308 of the Regulations will be made to reflect this amendment.

As a consequence of these amendments, it is also proposed to amend paragraph (*j*.1) of the definition of "remuneration" in subsection 100(1) of the *Income Tax Regulations* to ensure that an exemption from withholding on account of Part I tax applies in connection with distributions in a year from an RRIF that would be in respect of the minimum amount under the fund for the year if an assumption were made. The assumption is that each payment, scheduled at the beginning of the year to be paid after the time of the RRIF distribution and in the year into the fund under an annuity contract held in connection with the fund at the beginning of the year, is paid into the fund in the year.

These amendments generally apply to the 1998 and subsequent taxation years. However, the application of the amendment is subject to grandfathering that preserves some existing grandfathering that applies to certain pre-March 1986 plans.

Subclause 70(2)

"qualified investment"

The definition of "qualified investment" in subsection 146.3(1) sets out the types of property that a trust governed by an RRIF is permitted to hold. If a trust governed by an RRIF acquires or holds a property that is not a "qualified investment", there are generally unfavourable tax consequences for the RRIF annuitant under subsection 146.3(7) of the Act or the trust under Part XI.1 of the Act. Under the existing rules, an annuity contract is not a qualified investment for a trust governed by an RRIF.

Paragraphs (*b*.1) and (*b*.2) of the definition are added, effective after 1996, so that an RRIF trust can hold certain types of annuity contracts as qualified investments.

New paragraph (*b*.1) permits a trust governed by an RRIF to hold one type of annuity. The conditions that an annuity must satisfy to qualify under paragraph (*b*.1) are identical to the conditions that an annuity must satisfy under the new RRSP rules for qualified investments, described in the commentary on those provisions. Accordingly, where on maturity a trusteed RRSP holds such an annuity, it will be possible to transfer the annuity to an RRIF trust instead of disposing of it. An RRIF trust could also acquire such an annuity directly from an insurer.

New paragraph (*b*.2) permits an RRIF trust to hold a second type of annuity without penalty where the annuity satisfies six conditions:

- (1) periodic payments under the annuity contract are required to be made on an annual or more frequent basis;

- (2) the RRIF trust must be the only person that has the right to receive any annuity payments under the contract (unless the trust disposes of the annuity);

- (3) neither the time nor the amount of any payment under the contract can vary because of the length of any life, other than the life of the RRIF annuitant, except that where the annuitant under the fund has elected to have the carrier pay the minimum amount each year to the annuitant's spouse after the annuitant's death, the payments under the contract can be based on the joint lives of the annuitant and the annuitant's spouse;

- (4) the date on which the periodic payments began or are to begin must be no later than the end of the year following the year in which the contract was acquired by the trust;

- (5) the annuity contract must be either

    (a) a life annuity for the life of the RRIF annuitant or, where the RRIF annuitant had a spouse when the contract was acquired, for the joint lives of the RRIF annuitant and the RRIF annuitant's spouse, that does not have a guaranteed period that runs past the end of the year in which the RRIF annuitant attains 90 years of age, except that where the RRIF annuitant had a spouse at the time that the contract was acquired, the

guaranteed period, if any, can run up to the end of the year in which the spouse attains 90 years of age (if it is a later year), or

(b) a term annuity with a term equal to either 90 years minus the age of the RRIF annuitant at the date on which the periodic payments start or 90 years minus the age of the RRIF annuitant's spouse as of that date; and

- (6) the periodic payments must be equal unless

(a) they have been adjusted for reasons that would, if the contract were an annuity under a retirement savings plan, be in accordance with the indexing or other options provided under subparagraphs 146(3)(*b*)(iii) to (v), or

(b) they have been uniformly reduced as a consequence of a partial surrender of the right to receive periodic payments under the contract.

New paragraph (*c*.2) of the definition "qualified investment" in subsection 146(1) is very similar to new paragraph (*b*.2) of the definition "qualified investment" in subsection 146.3(1). An annuity that qualifies under paragraph (*c*.2) will generally qualify under the RRIF rules, thus making it possible to transfer such an annuity to an RRIF on the maturity of the RRSP that holds it.

Subclauses 70(3) to (5)

Registration

ITA
146.3(2)(*e*) to (*e*.2)

Subsection 146.3(2) of the Act sets out the conditions that a retirement income fund must meet before Revenue Canada will register the fund.

Paragraph 146.3(2)(*e*) sets out one condition for registration — that the arrangement between the carrier and the RRIF annuitant give the RRIF annuitant the right to direct the carrier to transfer the property held in connection with the fund to another carrier. However, this condition is subject to paragraph 146.3(2)(*e*.1) under which the carrier

must retain sufficient property to enable it to pay the "minimum amount" for the year to the annuitant. If this requirement were not imposed, the minimum amount might not be paid in the year of transfer as the original carrier would have no property with which to pay it and the minimum amount for that year in respect of the transferee fund could be nil because the minimum amount is based on the fair market value of the property held by a carrier at the beginning of a year.

Paragraph 146.3(2)(*e*) is amended to make the RRIF annuitant's right to demand a transfer of the property held in connection with the fund subject to either paragraph 146.3(2)(*e*.1) or new paragraph 146.3(2)(*e*.2), depending on the circumstances.

Paragraph 146.3(2)(*e*.1) is amended so that it applies to an RRIF that governs a trust only if the trust was created before 1998 and the trust does not hold an annuity contract as a qualified investment. In any other case where an RRIF governs a trust, new paragraph 146.3(2)(*e*.2) applies.

Like paragraph 146.3(2)(*e*.1), new paragraph 146.3(2)(*e*.2) essentially requires the carrier to retain sufficient property to enable it to pay the "minimum amount" for the year to the annuitant after the transfer. However, paragraph 146.3(2)(*e*.2) provides special rules dealing with the holding of annuity contracts as qualified investments. While annuities that can be surrendered for cash are treated in the same manner as other RRIF property, in the case of other annuities, the "fair market value" of the retained annuity is ignored. Instead, only the annuity payments estimated to be made after the transfer and in the year of the transfer will effectively be considered to have been retained by the RRIF trust for the purposes of new paragraph 146.3(2)(*e*.2).

These amendments apply to retirement income funds entered into after July 13, 1990, which is the date on which the withholding requirement under paragraph 146.3(2)(*e*) first applied.

Clause 71

Definitions

ITA
248(1)

"licensed annuities provider"

The definition "licensed annuities provider" is added to subsection 248(1) of the Act to make the definition of that term in subsection 147(1) generally applicable for all purposes of the Act. Under subsection 147(1), a "licensed annuities provider" is a person licensed or otherwise authorized under the laws of Canada or a province to carry on an annuities business in Canada.

The term is now used in the amended definitions of "qualified investment" in subsections 146(1) and 146.3(1).

This definition applies after 1996.

Division B

Clause 72

Income Tax Conventions Interpretation Act

ITCIA
5

"periodic pension payment"

Canada's tax treaties generally treat a "periodic pension payment" differently from a lump sum payment from a similar source. Section 5 of the Income Tax Conventions Interpretation Act (ITCIA) defines what constitutes a "periodic pension payment" for the purpose of Canada's tax treaties.

Paragraph (*c*) of the definition of "periodic pension payment" generally includes a payment received under a registered retirement

income fund (RRIF), unless the total of the payment (and all previous payments in the year under the RRIF) exceeds the greater of:

- twice what the "minimum amount" under the fund would be if the definition "minimum amount" applied to all RRIFs, including those entered into before March 1986, and

- 10% of the fair market value of the property held in connection with the fund at the beginning of the year.

Note that in calculating the above amounts, where property has been transferred to the carrier in the year before the particular payment is made, it is assumed that the transferred property was actually held in connection with the fund at the beginning of the year (referred to below as the "transfer assumption").

Paragraph (*c*) of the definition of "periodic pension payment" is amended so that the definition generally includes a payment made in the year under an RRIF, unless the total of the payment and all payments previously made in the year under the RRIF exceeds the total of:

- the greater of

  - twice what the minimum amount under the fund for the year would be if the transfer assumption were made, the definition "minimum amount" applied to all RRIFs, including those entered into before March 1986, and the value of C in that definition were nil, and

  - 10% of the fair market value of the property (other than any properties that are annuity contracts that cannot be surrendered for cash) held in connection with the fund at the beginning of the year, determined as if the transfer assumption were made, and

- the total periodic payments previously received by the RRIF trust in the year under annuity contracts held by the trust that are qualified investments (as defined by subsection 146.3(1) of the *Income Tax Act*) and that cannot be surrendered for cash.

This amendment is intended to ensure that, where an RRIF trust receives periodic payments under an annuity contract that it holds as a qualified investment, each payment flowed out to the RRIF annuitant is a "periodic pension payment".

Paragraph (*c*) excludes certain types, and portions of certain types, of RRIF payments. Paragraph (*c*) is also amended so that each type of RRIF payment ignored for the purpose of the existing rules is now described as a "specified portion" of an RRIF payment – a term that is defined in new subsection 5.1(2) of the ITCIA. This amendment does not represent a change in policy.

This amendment applies to amounts paid after 1997.

Clause 73

ITCIA
5.1

Paragraph (*c*) of the definition "periodic pension payment" in section 5 of the ITCIA excludes certain types, and portions of certain types, of RRIF payments from being periodic pension payments. Paragraph (*c*) is amended so that any portion of an RRIF payment excluded for the purpose of the existing rules is now described as a "specified portion" of an RRIF payment – a term that is defined in new subsection 5.1(2) of the ITCIA. The addition of this definition does not represent a change in policy. The ignored RRIF payments are those not required to be included in computing income and those for which "rollover" treatment is available under paragraph 60(*l*) of the *Income Tax Act*.

This amendment applies to amounts paid after 1997.

PART III

EXPLANATORY NOTES TO DRAFT AMENDMENTS RPP ANNUITIES

Clause 74

Deemed RPP registration

ITA
147.1(3)(*a*)

Paragraph 147.1(3)(*a*) of the *Income Tax Act* deems a pension plan that has been submitted to Revenue Canada for registration to be a registered pension plan until a final determination is made as to the plan's registration. However, it specifically provides that the deemed registered status of a pension plan does not apply for the purposes of certain provisions of the Act that would otherwise allow the tax-free transfer of funds to be made from the plan.

Paragraph 147.1(3)(*a*) is amended to provide that it also does not apply for the purposes of new section 147.4 of the Act. In general terms, that section allows an individual to acquire ownership of an annuity contract, in satisfaction of the individual's entitlement to benefits under a registered pension plan, without adverse tax consequences provided certain conditions are satisfied. Thus, an individual cannot acquire ownership of an annuity contract under a pension plan on a tax-neutral basis until the plan is actually registered.

This amendment applies after 1996.

Clause 75

RPP transfers

ITA
147.3

Section 147.3 of the Act provides rules governing the transfer of funds from registered pension plans (RPPs) to registered retirement savings plans (RRSPs), registered retirement income funds (RRIFs) and other RPPs.

Subclause 75(1)

Taxation of amount transferred

ITA
147.3(10)(*a*)

Subsection 147.3(10) of the Act provides rules that apply where an amount is transferred on behalf of an individual from an RPP to an RRSP, a RRIF or another RPP otherwise than in accordance with subsections 147.3(1) to (7) of the Act. In these circumstances, paragraph 147.3(10)(*a*) deems the amount to have been paid from the RPP directly to the individual, as a result of which it is included in the individual's income under paragraph 56(1)(*a*) of the Act. Paragraph 147.3(10)(*a*) specifically provides that it applies notwithstanding section 254 of the Act which, under certain circumstances, may have applied to exempt the amount from immediate taxation.

Paragraph 147.3(10)(*a*) is amended to delete the reference to section 254. This amendment is consequential on the introduction of new section 147.4 and the amendments to section 254. For further details, see the commentary on those provisions.

This amendment applies to transfers occurring on or after Announcement Date.

Subclause 75(2)

Annuity contract commencing after age 69

ITA
147.3(15)

Subsection 147.3(15) of the Act contains rules relating to annuities acquired by individuals before 1997 to provide benefits in lieu of their entitlement to benefits under an RPP. The rules apply in the event that payment of the annuity does not begin by the end of the year in which the individual turns 69 years of age. As a consequence of the introduction of section 147.4, which contains other provisions dealing with individually-owned annuity contracts, subsection 147.3(15) is renumbered as subsection 147.4(4).

This amendment applies from the time of the introduction of subsection 147.3(15) (after 1996).

Clause 76

RPP annuity contracts

ITA
147.4

Section 147.4 of the Act provides a new set of rules that deal primarily with individuals acquiring ownership of annuity contracts in satisfaction of their entitlement to benefits under an RPP.

Subsection 147.4(1) replaces, in modified form, the mechanism provided under paragraph 254(*a*) for individuals to acquire annuities under superannuation or pension funds or plans without adverse consequences. It restricts the application of the relief previously afforded by paragraph 254(*a*) to annuities acquired under RPPs.

Subsections 147.4(2) and (3) provide rules that apply where an annuity contract to which subsection 147.4(1) or paragraph 254(*a*) applies is amended or replaced.

Subsection 147.4(4) is simply a renumbering of existing subsection 147.3(15).

Subclause 76(1)

Acquisition of RPP annuity contracts

ITA
147.4(1)

Subsection 147.4(1) of the Act applies where an individual acquires ownership of an annuity contract in satisfaction of the individual's entitlement to benefits under an RPP. This might occur, for example, where a plan discharges its benefit obligations with respect to an individual either by transferring ownership of an existing annuity contract held in connection with the plan to the individual or by purchasing an annuity contract under which the individual is both the annuitant and the owner. Under these circumstances, the individual is deemed not to have received an amount from the RPP as a result of acquiring the annuity and any amounts received under the contract are deemed to be amounts received under the RPP. As a consequence, there is no immediate taxation on acquisition of the annuity and any payments under the contract are included in the recipient's income in the year in which they are received.

Subsection 147.4(1) provides that these deeming rules apply with respect to the acquisition of an RPP annuity contract only if the following conditions are met:

- the rights provided for under the contract are not materially different from those provided for under the RPP;

- the contract does not provide for any further premiums to be paid after it is acquired by the individual; and

- at the time of acquisition, the registration of the plan is not revocable. However, under subsection 147.4(1), the Minister of National Revenue has the authority to ignore the fact that the registration of the plan is revocable. It is generally expected that the Minister would do so where there is no connection between the cause of the plan being revocable and the benefits being provided by way of the annuity.

Also, subsection 147.4(1) provides that the deeming rules do not apply where an individual acquires an interest in an annuity contract by way of a transfer to an RRSP or RRIF. In such cases, the rules governing inter-plan transfers in section 147.3 apply.

Subsection 147.4(1) is intended to protect annuity acquisitions only where the rights provided for under the annuity contract are the same as the rights provided for under the RPP (ignoring any immaterial differences). It is not intended to allow a plan member to reconfigure the amount or modify the form of the benefits provided for under the plan. Plan members who want such flexibility can achieve this by transferring the value of their pension entitlements to an RRSP or RRIF (within the constraints of section 147.3 of the Act).

Where an individual acquires ownership of an annuity contract under an RPP otherwise than in accordance with subsection 147.4(1), the individual is considered to have received a payment in kind from the RPP and is required to include the value of the contract in income under paragraph 56(1)(*a*) of the Act.

Subsection 147.4(1) applies to contract acquisitions occurring on or after Announcement Date.

The following are examples of RPP annuity acquisitions that do not satisfy the conditions for the deeming rules in subsection 147.4(1) to apply.

Example 1

On retirement, Catherine, a member of a defined benefit RPP is entitled to an indexed pension of $20,000 per year. Under the terms of the plan, Catherine is given the option of either transferring the value of her benefits to a locked-in RRSP (subject to the transfer limits) or acquiring from a life insurance company an indexed annuity of $20,000 per year. Catherine elects the annuity option, but foregoes the indexing in exchange for additional lifetime annuity payments of $5,000 per year (an option that was not provided for under the plan). Subsection 147.4(1) does not protect the acquisition of the annuity contract since it provides for rights that are materially different from those provided for under the RPP.

It should be noted that, had the plan allowed Catherine to give up indexing in exchange for higher lifetime retirement benefits, Catherine's pension adjustments under the plan would have been calculated based on those higher lifetime retirement benefits.

Example 2

A money purchase RPP has not been amended to reduce the latest time for a member's pension to commence from the end of the year in which the member turns 71 years of age to the end of the year in which the member turns 69 years of age. At retirement, a 65 year old member, David, acquires ownership of an annuity contract that provides for commencement at age 71. Since the plan is revocable for failing to comply with the registration requirements for pension commencement, David's acquisition of the annuity is not protected by subsection 147.4(1). This is not a situation in which Revenue Canada would be expected to ignore the fact that the registration of the plan is revocable.

Subclause 76(2)

Amended contract

ITA
147.4(2)

New subsection 147.4(2) of the Act contains rules relating to amendments to annuity contracts to which subsection 147.4(1) or paragraph 254(*a*) of the Act applies. The rules apply if the rights provided for under the contract are materially altered as a consequence of the amendment. In such a case, an individual with an interest in the contract immediately before the amendment is deemed to have received an amount from a pension plan equal to the fair market value of that interest. By virtue of paragraph 56(1)(*a*) of the Act, the individual is required to include this amount in income.

Subsection 147.4(2) also deems the amended contract to be a separate annuity contract. Consequently, paragraph 147.4(1)(*g*) or 254(*a*) cease to apply to payments made under the contract. The contract is also deemed not to have been issued pursuant to or under a superannuation or pension fund or plan. This ensures that the amended contract is not a prescribed annuity contract by virtue of

paragraph 304(1)(*a*) of the *Income Tax Regulations* and may thus be subject to the accrual rules in section 12.2 of the Act. Finally, an individual with an interest in the amended contract is deemed to have acquired the interest at the time of the amendment at a cost equal to the fair market value of that interest immediately after the amendment. This establishes the date of acquisition and the adjusted cost basis for purposes of the accrual rules.

Subsection 147.4(2) does not apply where an annuity contract is amended to provide for an earlier annuity commencement date in order to avoid the application of subsection 147.4(4).

Subsection 147.4(2) applies to contract amendments occurring on or after Announcement Date.

Subclause 76(3)

New contract

ITA
147.4(3)

New subsection 147.4(3) of the Act contains rules relating to annuity contracts that replace contracts to which subsection 147.4(1) or paragraph 254(*a*) applies. As long as the rights provided for under the new contract are not materially different from those provided for under the original contract, the new contract is considered to be the same contract as the original contract. As a result, any annuity payments received under the new contract will be treated as superannuation or pension benefits by virtue of paragraph 147.4(1)(*g*) or 254(*a*).

However, where the rights are materially different, an individual with an interest in the original contract is deemed to have received an amount from a pension plan equal to the fair market value of that interest. By virtue of paragraph 56(1)(*a*) of the Act, the individual is required to include this amount in income. Since the replacement contract is a new contract, neither subsection 147.4(1) nor paragraph 254(*a*) applies with respect to annuity payments received under the contract. As a result, the new contract is subject to the tax treatment that would normally apply to an annuity contract that is not issued pursuant to a pension plan.

New subsection 147.4(3) applies to contract replacements occurring on or after Announcement Date.

Subclause 76(4)

Annuity contract commencing after age 69

ITA
147.4(4)

Subsection 147.3(15) of the Act is renumbered as subsection 147.4(4). Subsection 147.3(15) deals with individually-owned RPP annuity contracts that were acquired before 1997 and under which payments do not begin by the end of the year in which the individual turns 69 years of age. This renumbering is consequential on the introduction of section 147.4.

Clause 77

Contract under pension plan

ITA
254

Section 254 of the Act contains rules that apply where a contract is issued in satisfaction of an individual's rights under a pension plan. Paragraph 254(*a*) provides that, where the rights provided under the contract are rights provided under the plan, any payment made under the contract is considered to be a payment from the plan. By virtue of paragraph 56(1)(*a*), such payments are included in the recipient's income for the year in which they are received. Paragraph 254(*a*) also ensures that there is no immediate taxation by deeming the individual not to have received a payment from the plan as a consequence of the contract being issued. Where the rights provided under the contract are not rights provided under the plan, paragraph 254(*b*) deems the individual to have received from the plan an amount equal to the value of those rights. The individual is required, by virtue of paragraph 56(1)(*a*), to include that amount in income for the year in which the contract is issued.

Section 254 is amended to restrict its application to contracts issued before Announcement Date. Similarly, paragraph 254(*a*) is amended so that it applies only where an individual acquired an interest in a contract before Announcement Date. This change is consequential on the introduction of new subsection 147.4(1) of the Act, which deals with annuity contracts acquired on or after Announcement Date. It should be noted that an amendment to a contract to which paragraph 254(*a*) applies will be subject to new subsection 147.4(2) if it materially alters the rights under the contract. The consequences of the application of that subsection are that there is an immediate income inclusion and paragraph 254(*a*) ceases to apply to payments made under the contract. It should also be noted that, where a contract to which paragraph 254(*a*) applies is replaced by a new contract, new subsection 147.4(3) provides that payments under the new contract continue to be subject to paragraph 254(*a*) so long as the rights under the two contracts are not materially different. For further details, see the commentary on section 147.4.

Finally, it should be noted that new subsection 147.4(1) applies only to contracts acquired in satisfaction of benefits provided to an individual under a registered pension plan. Consequently, neither paragraph 254(*a*) nor subsection 147.4(1) apply to defer immediate taxation in respect of annuity contracts acquired on or after Announcement Date under unregistered pension arrangements.

PART IV

EXPLANATORY NOTES TO DRAFT AMENDMENTS MATCHABLE EXPENDITURES

Clause 78

Proceeds of disposition of right to receive production

ITA
12(1)(g.1)

Proposed paragraph 12(1)(*g*.1) of the *Income Tax Act* requires proceeds of disposition of a right to receive production to which new subsection 18.1(6) of the Act applies to be included in calculating the income of the vendor. This amendment applies to dispositions that occur after November 17, 1996.

Clause 79

Matchable Expenditures

ITA
18.1

Proposed section 18.1 of the Act restricts the deductibility of an otherwise deductible matchable expenditure incurred in respect of a right to receive production by prorating the deductibility of the amount of the expenditure over the economic life of the right. This section does not create an entitlement to deduct an amount in respect of an expenditure, unless the expenditure is otherwise deductible under existing jurisprudence. The "Backgrounder" accompanying Department of Finance News Release 96-082 dated November 18, 1996 provides general details about the tax policy concerns that lead to section 18.1 being proposed by the government. Generally, these policy objectives concern the use of royalty-type arrangements to effect tax-assisted financing by structuring the arrangements as tax shelters or as debt substitutes. The detailed rules in section 18.1 are

discussed below. Generally, section 18.1 applies after November 17, 1996.

Subclause 79(1)

ITA
18.1(1)

Subsection 18.1(1) provides the definitions of the expressions "matchable expenditure", "right to receive production", "tax benefit", "tax shelter" and "taxpayer" for the purposes of section 18.1.

ITA
18.1(2) to (4)

Subsection 18.1(2) provides that matchable expenditures are deductible only to the extent provided by subsection 18.1(3).

Subsection 18.1(3) provides that a matchable expenditure is deductible in computing a taxpayer's income for a taxation year to the extent of the amount that is determined under subsection 18.1(4). However, subsection 18.1(4) does not apply to provide a deduction in computing income for a taxation year unless the taxpayer's matchable expenditure would otherwise have been deductible in that or another taxation year.

Subsection 18.1(4) provides rules for determining the amount of a taxpayer's matchable expenditure that may be deducted under subsection 18.1(3) if that provision applies. That amount is determined as the least of three amounts.

Generally, the first of those amounts is the expenditure pro-rated over the term of the right to receive production to which the expenditure relates, except that in no event is the term used to be less than 5 years. Added to this amount, however, are amounts that would have been deductible in preceding years under this computation but for the second constraint. The second constraint is the amount of income included in computing the taxpayer's income in respect of the right for the year. Added to this amount, however, is income for previous years against which amounts could not be deducted because of the first constraint. The third constraint is the amount that would otherwise have been deductible in computing the taxpayer's income

up to and including the current taxation year in respect of the taxpayer's right to receive production minus the amounts deductible under subsection 18.1(3) in computing the taxpayer's income for preceding taxation years. Two examples illustrating the application of these constraints follow the explanatory notes to proposed subsections 18.1(8) to (12).

ITA
18.1(5)

Subsection 18.1(5) of the Act provides four special rules that apply for the purposes of section 18.1. First, if a taxpayer's matchable expenditure is made before the related right to receive production is acquired, the expenditure will be considered to have been made on the day that the right is acquired. Second, if a taxpayer has one or more rights to renew a right to receive production for one or more additional terms, the term of the right is to be treated as terminating at the latest possible time that such an additional term could terminate if all rights to renew the right were exercised. Third, where a taxpayer has two or more rights to receive production that can reasonably be considered to be related to each other, the rights are treated as one right. Fourth, if the term of a taxpayer's right to receive production is for an indeterminate period, the right is considered to terminate 20 years after it is acquired.

ITA
18.1(6) to (7)

Subsection 18.1(6) provides that a taxpayer's proceeds of disposition of a right to receive production are to be included in computing the taxpayer's income.

Subsection 18.1(7) provides that, upon disposition or expiry, a taxpayer may claim a terminal deduction in respect of a right to receive production to which a matchable expenditure relates. However, this terminal deduction is not available where subsection 18.1(8) or (9) applies.

ITA
18.1(8) to (12)

Subsection 18.1(8) defers a taxpayer's terminal deduction in respect of a disposed of or expired right to receive production in certain cases involving non-arm's length parties. In such cases, a taxpayer's terminal deduction is governed by subsection 18.1(10).

Subsection 18.1(9) describes a special arm's length case in which a taxpayer's terminal deduction otherwise available under subsection 18.1(7) in respect of a disposed of or expired right to receive production is deferred. If applicable, an affected taxpayer's deductions are to be computed under subsection 18.1(10). In particular, subsection 18.1(9) applies where, during the 30-day period that begins at the time of disposition or expiry, a taxpayer that had a direct or indirect interest in the right has a direct or indirect interest in any other right to receive production, which other interest is a tax shelter or a tax shelter investment (as defined by section 143.2 of the Act). For example, this condition precludes Partnership 1 from claiming a terminal deduction in respect of its right to receive production if another partnership (i.e., Partnership 2) that has (or had) an interest in Partnership 1 has an interest, directly or indirectly, in any other right to receive production and the other interest is a tax shelter or a tax shelter investment (e.g., Partnership 3 holds a right and Partnership 2 has (or had) an interest in Partnership 1 and has a partnership interest in Partnership 3 that is a "tax shelter investment").

Paragraph 18.1(10)(*a*) provides the rule for deducting matchable expenditures during the period to which subsection 18.1(8) or (9) applies. During that period, paragraph 18.1(10)(*a*) limits a taxpayer's deduction in respect of a matchable expenditure to an amount that cannot exceed the least of the three amounts described in subsection 18.1(4).

Paragraph 18.1(10)(*b*) provides for a terminal deduction for a matchable expenditure in respect of a disposed of or expired right to receive production at the earliest of certain subsequent times. These times are

- the time at which the right would, if owned by the taxpayer, be deemed by section 128.1 (change of residence) or

subsection 149(10) (change of taxable status) to have been disposed of by the taxpayer;

- the time that is immediately before control of the taxpayer is acquired by a person or group of persons, if the taxpayer is a corporation;

- the time at which winding-up of the taxpayer begins (other than a winding-up to which subsection 88(1) of the Act applies), if the taxpayer is a corporation;

- where subsection 18.1(8) applies, the time at which a 30-day period begins throughout which neither the taxpayer nor an affiliated or non-arm's length person owns

  - the substituted property (referred to in subsection 18.1(8)), or

  - a property that is identical to the substituted property and that was acquired no earlier than 30 days before the period begins; or

- where subsection 18.1(9) applies, the time at which a 30-day period begins throughout which no taxpayer who had a direct or indirect interest in the right has a direct or indirect interest in another right to receive production, which other interest is a tax shelter or a tax shelter investment (as defined by section 143.2 of the Act).

Subsection 18.1(11) of the Act clarifies the result where a right to receive production expires or is disposed of by a partnership that subsequently ceases to exists. Where a partnership would otherwise cease to exist after a disposition or expiry of a right to which subsection 18.1(10) of the Act applies, the partnership is treated as not having ceased to exist, and each taxpayer who was a member of the partnership at the time of the disposition or expiry is treated as having remained a member of the partnership. This deemed continuation of the partnership (and of the membership of each partner) continues until the time that is immediately after the first of the events that trigger the partnership's terminal deduction in respect of the matchable expenditure.

Subsection 18.1(12) of the Act provides that, for the purpose of the substituted property rule in subsection 18.1(8) and (10), a "right" to acquire a right to receive production is identical to the right to receive production. This rule does not apply to a "right", as security only, derived from a mortgage, agreement of sale or similar obligation.

Example 1: Taxpayer Holds Right until Expiry

- Taxpayer A incurs $1,000 of matchable expenditures that relate to a right to receive production from Taxpayer B's business over a 6-year period (i.e., 25% of the annual gross sales from the sale of a particular product).

- The $1,000 was expended for the purpose of earning income. Taxpayer A has a reasonable expectation of profit from the right to receive production, and the amount is otherwise deductible. The deductibility of the matchable expenditure is, therefore, provided for by subsection 18.1(3) of the Act (as determined under subsection 18.1(4)).

- Taxpayer A receives the following gross revenue payments from Taxpayer B:

  Year 1: $100
  Year 2: $200
  Year 3: $300
  Year 4: $200
  Year 5: $100
  Year 6: $500

- Taxpayer A's right to receive production expires in year 6 (i.e., subsection 18.1(7) applies in that year).

Calculation of Taxpayer A's Subsection 18.1(3) Deduction:

Year 1: Taxpayer A may deduct $100 pursuant to subsections 18.1(3) and (4), being the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- Nil
  $167

(b): the total of

- $100 (receipts included in income)

- Nil
  $100

(c): $200 ($200 - Nil)[1]

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[1] Assuming a 5-year matching period under general principles.

Year 2: Taxpayer A may deduct $200 which is the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- $ 67 (year 1: $167(a) - $100(b))
  $234

(b): the total of

- $200 (receipts included in income)

- Nil
  $200

(c): $300 ($400 - $100)

Year 3: Taxpayer A may deduct $201 which is the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- $ 34 (year 2: $234(a) - $200(b))
  $201

(b): the total of

- $300 (receipts included in income)

- Nil
  $300

(c): $300 ($600 - $300)

Year 4: Taxpayer A may deduct $167 which is the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- Nil
  $167

(b): the total of

- $200 (receipts included in income)
- $ 99 (year 3: $300(b) - $201(a))
  $299

(c): $299 ($800 - $501)

Year 5: Taxpayer A may deduct $167 which is the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- Nil
  $167

(b): the total of

- $100 (receipts included in income)

- $132 (year 4: $299(b) - $167(a))
  $232

(c): $332 ($1,000 - $668)

Year 6: Taxpayer A may deduct $165 because subsection 18.1(7) applies. The amount otherwise determined under subsection 18.1(4) would have been the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- Nil
  $167

(b): the total of

- $500 (receipts included in income)

- $ 65 (year 5: $232(b) - $167(a))
  $565

(c): $165 ($1,000 - $835)

SUMMARY

Year	Income	Deductible Portion of Matchable Expenditure	Net Income (loss)
1	$100	$ 100	Nil
2	$200	$ 200	Nil
3	$300	$ 201	$ 99
4	$200	$ 167	$ 33
5	$100	$ 167	($ 67)
6	$500	$ 165	$335
Total		$1,000	

Example 2: Taxpayer Disposes of Right to Affiliated Person

- Taxpayer A incurs $1,000 of matchable expenditures that relate to a right to receive production from Taxpayer B's business over a

6-year period (i.e., 25% of the annual gross sales from the sale of a particular product).

- The $1,000 amount was expended for the purpose of earning income, Taxpayer A has a reasonable expectation of profit from the right to receive production and the amount is otherwise deductible (subject to matching) under previously existing jurisprudence. The deductibility of the matchable expenditure is, therefore, provided for by subsection 18.1(3) (as determined under subsection 18.1(4)).

- For years 1 to 4, Taxpayer A receives the following gross revenue payments from Taxpayer B:

  Year 1: $100
  Year 2: $200
  Year 3: $300
  Year 4: $200

- In year 4, and after receiving the $200 from Taxpayer B, Taxpayer A disposes of the right to receive production for nil proceeds to affiliated person C (assume that the transfer of the right occurred at fair market value and that the attribution rules do not apply to any potential receipts that affiliated person C may receive from the right).

- Affiliated person C's acquired right to receive production expires at the end of year 6.

Calculation of Taxpayer A's Subsection 18.1(3) Deduction:

Years 1 to 3: See Example 1 above (i.e., Year 1 = $100; Year 2 = $200; and Year 3 = $201).

Year 4: Taxpayer A may deduct $167 which is the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- Nil
  $167

(b): the total of

- $200 (receipts included in income)

- $ 99 (year 3: $300(b) - $201(a))
  $299

(c): $499 ($1,000 - $501)

Year 5: Taxpayer A may deduct $132 which is the least of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- Nil
  $167

(b): the total of

- Nil (receipts included in income)

- $132 (year 4: $299(b) - $167(a))
  $132

(c): $332 ($1,000 - $668)

Year 6: Taxpayer A may deduct $200 because paragraph 18.1(10)(*b*) applies to deem the amount determined under subsection 18.1(4)(*c*) to be the relevant amount for the year notwithstanding that the amount otherwise determined under proposed paragraph 18.1(4)(*b*) would have been the least amount of:

(a): the total of

- the lesser of
  $200 (1/5 x $1,000)
  $167 ($1,000/6)

- $ 45 (Year 5: $167(a) - $132(b))
  $212

(b): the total of

- Nil

- Nil
  Nil

(c): $200 ($1,000 - $800)

SUMMARY

Year	Income	Deductible Portion of Matchable Expenditure	Net Income (loss)
1	$100	$ 100	Nil
2	$200	$ 200	Nil
3	$300	$ 201	$ 99
4	$200	$ 167	$ 33
5	Nil	$ 132	($132)
6	Nil	$ 200	($200)
Total		$ 1,000	

ITA
18.1(13)

Subsection 18.1(13) provides that a matchable expenditure is considered to be a tax shelter investment for the purpose of applying the limited-recourse debt rules in proposed section 143.2 of the Act. For this purpose, however, the limited-recourse debt rules are to be read without reference to the "at-risk adjustment" reductions.

ITA
18.1(14)

Subsection 18.1(14) provides that a right to receive production is considered to be a debt obligation to which the accrual rules in Part LXX of the *Income Tax Regulations* apply if the rate of return on the right is reasonably certain. In such cases, no amount may be deducted under subsection 18.1(3) of the Act in respect of any matchable expenditure that relates to the right.

ITA
18.1(15)

Subsection 18.1(15) describes those matchable expenditures in respect of a right to receive production that are not subject to the new matchable expenditure rules in section 18.1. This rule applies only if no portion of a taxpayer's expenditure can reasonably be considered to have been paid to another taxpayer to acquire the right from the other taxpayer. In addition, the taxpayer's expenditure must be such that either

- the expenditure does not relate to a tax shelter and none of the main purposes for making the expenditure is that the taxpayer obtain a tax benefit, or

- before the end of the taxation year in which the expenditure is made, the total income inclusions of the taxpayer from the right to receive production to which the expenditure relates exceeds 80% of the expenditure.

For example, a taxpayer that manages another person's property in return for a fee that is computed in whole or in part with reference to the value of the property being managed (i.e., the right to receive the

fee is a right to receive production) may incur matchable expenditures in respect of the right. Nevertheless, the matchable expenditure rules will not apply to the taxpayer's expenditures in respect of the right where the conditions in subsection 18.1(15) apply. This would be the case, for example, where

- no portion of the expenditure in respect of the right can reasonably be considered to have been paid by the taxpayer/manager to acquire the right from the other person, and

- the taxpayer/manager's expenditure in respect of the right does not relate to a tax shelter or a tax shelter investment (as defined by section 143.2 of the Act) and none of the main purposes for making the expenditure is that the taxpayer, or a person with whom the taxpayer does not deal at arm's length, obtain a tax benefit.

Clause 80

Amalgamations

ITA
87(2)(*j*.2)

Paragraph 87(2)(*j*.2) of the Act provides that a corporation formed as a result of an amalgamation is considered to be a continuation of its predecessor corporations for the purposes of subsection 18(9) (prepaid expenses), subsection 18(9.01) (premium paid under group life insurance policies) and paragraph 20(1)(*mm*) (cost of injected substance used to recover petroleum, natural gas or related hydrocarbons). Paragraph 87(1)(*j*.2) is amended, effective November 18, 1996, so that it also applies for the purpose of new section 18.1 (i.e., to a right to receive production to which a matchable expenditure relates).

Clause 81

Windings-Up

ITA
88(1)(*a*)(i)

Paragraph 88(1)(*a*) of the Act provides rules for determining the proceeds of disposition of a subsidiary's property a on wind-up to which subsection 88(1) applies. Subparagraph 88(1)(*a*)(i) is amended to provide nil proceeds of the disposition of a subsidiary's right to receive production to which a matchable expenditure relates. This effectively results in a rollover of a subsidiary's right to receive production to its parent. This subsection applies after November 17, 1996.

Clause 82

Definitions

ITA
248(1)

Subparagraph (*e*)(iv) of the definition of "cost amount" in subsection 248(1) of the Act is amended consequential on the rules that apply to a right to receive production to which a matchable expenditure relates ("right to receive production" and "matchable expenditure" are defined in new section 18.1). This subsection applies after November 17, 1996.

Clause 83

Acquisition of Control

ITA
256(7)

Subsection 256(7) of the Act describes circumstances in which control of a corporation will be treated as not having been acquired for the purposes of certain provisions. Subsection 256(7) is amended

to add a reference to new section 18.1 (relating to matchable expenditures) so that in the circumstances described in subsection 256(7) control of a corporation will not be considered to have been acquired for the purpose of subparagraph 18.1(10)(*b*)(ii). This amendment applies after November 17, 1996.

SCHEDULE II

EXPLANATORY NOTE TO DRAFT AMENDMENT

APPLICATION RULE FOR SUBSECTIONS 112(3) TO (3.32) OF THE *INCOME TAX ACT*, AS PROPOSED IN BILL C-69

Bill C-69 was tabled in the previous Parliament on November 20, 1996. The House of Commons did not pass Bill C-69 before Parliament dissolved in April 1997. In order to take effect, these provisions must be reintroduced in a new bill when the new session of Parliament begins in the fall. The following notes explain changes that are to be made to the provisions of Clause 57 of Bill C-69.

Clause 57 of Bill C-69 provides rules which reduce a taxpayer's loss arising on the disposition of a share of the capital stock of a corporation by the amount of certain dividends received by the taxpayer on the share. These rules generally apply to share dispositions that occur after April 26, 1995. They do not apply, however, to share dispositions that occur in the situations described in clause 57(10) of Bill C-69. That clause is amended in several ways. First, the amendment removes the requirement in clause 57(10)(*b*) that the disposition of a share be made pursuant to a written agreement entered into before April 1997.

Second, the requirement in clause 57(10)(*b*), that it be reasonable to conclude that the proceeds of a life insurance policy be primarily intended to fund a share redemption, will be modified. Under the modified clause 57(10)(*b*), the transitional relief may apply provided that a main purpose of the life insurance policy was to fund a share redemption. This change is intended to expand the types of circumstances which can qualify for transitional relief.

Third, the share ownership requirement in clause 57(10) is modified to include shares owned on April 26, 1995 by a trust under which an individual is a beneficiary. Therefore, the transitional rule in clause 57(10)(*b*) may apply where: the shares are owned by a trust on April 26, 1995; a corporation was a beneficiary of a life insurance policy on the life of an individual beneficiary (or the individual's spouse) of the trust; a main purpose of the insurance was to fund a

redemption of the shares; and the share disposition is made by the individual, the individual's spouse or their estates.

Fourth, modified clause 57(10)(*b*)(i) and new clause 57(10)(*b*)(iv)(C) will ensure that transitional relief is available where

- a share was owned by a spousal trust on April 26, 1995;
- a corporation was a beneficiary of a life insurance policy that insured the life of the beneficiary spouse under the trust;
- a main purpose of the insurance policy was to fund a redemption of the share; and
- the share is disposed of by the spouse trust to the corporation after the spouse's death and before the end of the trust's third taxation year that begins after the spouse's death.

Fifth, the transitional rule will be amended to clarify that the disposition of a share may qualify for transitional relief where the disposition is made by the individual whose life was insured, the individual's spouse or their estates. The transitional rules are also expanded to include certain share dispositions made by inter vivos or testamentary spouse trusts created by the individual whose life (or whose spouse's life) was insured on April 26, 1995.

In addition to these changes, the supporting rule in clause 57(11) of the Bill will be modified. For the purposes of clause 57(10)(*b*), existing clause 57(11) provides that a share acquired in exchange for another share on a conversion, transfer to a corporation, corporate reorganization or amalgamation to which section 51, 85, 86 or 87 (respectively) of the *Income Tax Act* applies is to be treated as being the same as the exchanged share for the purposes of

(i) determining whether a particular taxpayer owned the share on April 26, 1995; and

(ii) determining whether it was reasonable to conclude that a life insurance policy was intended to be used primarily to fund a redemption of the share.

Clause 57(11) will be simplified as a consequence of the changes to clause 57(10). A share acquired in exchange for another share in a transaction to which section 51, 85, 86 or 87 of the Act applies will be considered to be the same share as the exchanged share for all purposes of the rule in clause 57(10)(*b*). The amendment to clause 57(11) will also clarify that the transitional rule will continue to be available where there is a succession of share transfers, conversions, reorganizations or amalgamations.